Probiotec Annual Report 2012

WHAT WE DO

PROBIOTEC IS A LEADING DEVELOPER, MANUFACTURER AND DISTRIBUTOR OF PRESCRIPTION AND OVER-THE-COUNTER (OTC) PHARMACEUTICALS AND CONSUMER HEALTH PRODUCTS IN AUSTRALIA AND GLOBAL MARKETS.

Contents

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CHAIRMAN AND CEO'S LETTER TO SHAREHOLDERS

Dear fellow shareholders,

Your Board is pleased to present herewith the annual report of the company for the 2012 year. It is fair to say that after a couple of very tough years, the Board is pleased that the company is showing good signs of turning around its financial performance for the better, and it has a very confident view about the immediate future outlook for the business. For the year under review, the business has returned to profitability, and just as importantly, has generated good cash flow and reduced bank debt (as we forecast in last year's letter to shareholders). We see these as positive markers for the business as we enter the new financial year.

Past company reports and releases have detailed the Board and management's resolve to take a hard look at the business and reset its strategic imperatives and actions. This has seen a good number of initiatives over the past 18 months, the most important of which was the immediate cessation of our higher risk ventures, where the time lines to success were considered too great a cost to bare. These have all been completed. We also reset the company's business focus to ensure future success and growth, and in so doing, also took the opportunity to expediently dispose of one of the brands in our portfolio, "Milton", when it was obvious that there was a very keen buyer for that brand. Finally we embarked upon a programme of selling off surplus and non-core assets and operations, which to date has included our property in Queensland with an associated small business unit. This programme is ongoing with several properties and business units still potentially earmarked for sale, if satisfactory pricing can be achieved.

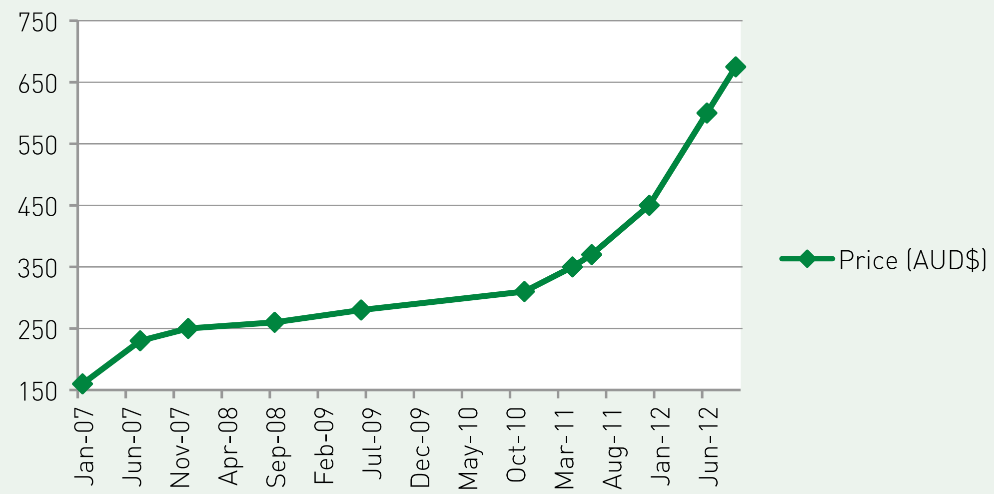
The result of this strategic review has been to put the business on a sound financial footing, with an ability for the management team to focus on those core profitable undertakings of the business that we see as capable of delivering both strong profit and strong future growth. We do have an excellent suite of branded pharmaceutical and health and wellbeing products in our portfolio, that already deliver strong margin and growth. However, we see additional growth potential for our existing brands, from both range extension and greater distribution reach. None more so obvious than with our flagship Celebrity Slim weight loss program. Up until the end of FY2012, our Celebrity Slim brand had been sold exclusively through the Priceline pharmacy chain. This arrangement worked well for both businesses for many years, but it was time to change the sales model for this brand. Consequently from the end of the first quarter of FY2013, you will see a massive expansion in the retail ranging of this product . Quite simply, this brand has been eagerly taken up by the major retailers in Australia, along with the wider pharmacy community. This new demand for access to the Celebrity Slim brand has led to a surge in orders as you would expect and the product will be visible to a large new customer base. We are confident that this is just one of a whole raft of similar successful initiatives, involving both range expansion and focus on distribution improvement, which will ensure the continuing improved performance of the business.

Another key plank of our strategic review was to acknowledge our expertise and very good performance in contract manufacturing of pharmaceutical products across a broad range of different products. Knowing that we successfully contract manufacture for the largest of global pharmaceutical companies, and that we are doing an ever increasing range of products for those same companies, puts us in good stead to market our capabilities in this regard, and search out further opportunities . And the business is coming our way. With continued contraction and rationalisation within the pharmaceutical manufacturing industry in Australia, we are constantly being approached to contract manufacture new products. Not everybody wants everything made offshore, and thus Probiotec is well placed to act as a contract manufacturing point for those customers that want local sourcing from an excellent factory that employs the highest of quality controls and standards. Therefore we are very bullish about our ability to steadily grow this part of our business over the coming years. In recent months we re-signed for 5 years of contract manufacture with one of those global pharmaceutical giants, which confirms the outside view about our state of readiness to perform.

With regards to our exporting activities, we continue to manage our weight loss business in the UK and Ireland. This includes our manufacturing facility in Ireland, with the bulk of our sales and marketing activities in the UK. To date the business here has shown enough promise for us to continue persevering with it, despite the depressed state of the Irish and British economies and despite the unfavourable exchange rate regime that we endure. In fact in recent months we have achieved some major new distribution placements for the Celebrity Slim product range in the UK, not dissimilar to what we have recently achieved in Australia. This has seen a surge in new orders and the Ireland factory comfortably busy.

Finally, we are excited about our future business profile in relation to dairy protein fractions. There are two sides to this business for us. Firstly after a number of years without a suitable home, we are pleased that within 6 months we will be commissioning our dairy protein fractionation plant in South Australia, in conjunction with our commercial partners United Dairy Power Pty Ltd. This is expected to see first production of Lactoferrin and Immunoglobulins in the first quarter of calendar 2013 and add a very valuable manufacturing arm to the Probiotec business. World Lactoferrin prices have been surging upwards for several years and show no signs of abating. In association with the production of these dairy fractions, Probiotec continues to progress what we expect to be ground breaking clinical trials using these fractions. We see this as very much the "blue sky" element to our future growth and prosperity, with the probability of success improving as we get closer to the day of commissioning the new plant in South Australia. This new business undertaking in South Australia is forecast to be almost immediately profit contributing, given the current strong international Lactoferrin price.

Lactoferrin Price Summary (per kg)



I hope that through the foregoing we have instilled shareholders with a sense of optimism about the future. It has of course been a disappointment to the Board to see the financial performance of the last few years erode the share price to historic lows. However we believe we have turned the corner and that it won't be long until the company is viewed upon more favourably than it has in the recent past. We are conscious that delivery of sound financial performance, not words, is what is now required, and we are set on doing just that.

We take this opportunity to thank the management team and the wider employee group at Probiotec for their very significant and much appreciated efforts in refocusing and rebuilding the Probiotec business, and to our fellow directors for their passionate contribution to the ongoing betterment of the business.

Maurice Van Ryn
Chairman

Wayne Stringer
CEO

OUR PERFORMANCE

SALES REVENUE

$66.5m

Significantly impacted by the discontinuance of a number of non-core and loss making operations, together with a continued decline in sales of the Group's meal replacement weight loss ranges.

NPAT (Excluding Impairment Costs)

$2.6m

This result shows what the directors believe to be the beginning of a sustained improvement in the performance of the Group. Despite the difficult economic conditions (highlighted by continued weakness in the retail environment), the Group has made a return to profitability in its underlying business.

FREE CASH FLOWS

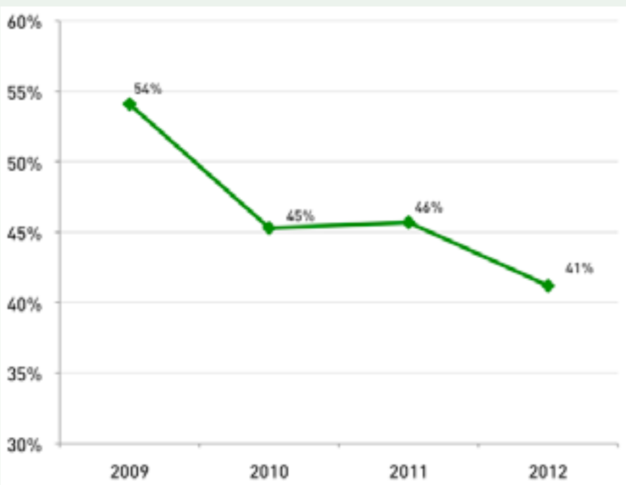
$4.7m

Free Cash Flows (defined as cash flow from operations plus cash flow from investing activities) derived from a combination of an improvement in working capital levels together with the financial benefits flowing from the implementation of the strategic initiatives (most notably, the sale of the Milton brand).

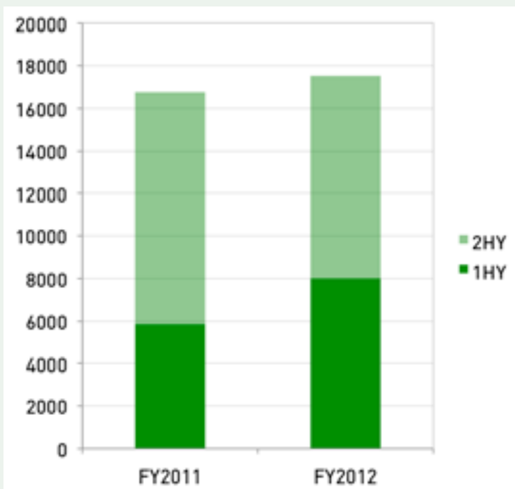
WINS FOR 2012

Milton sale	Sale of the Milton brand completed with a resultant net profit of $1.8m
Debt reduced	Net debt reduced by $4.7m
Reduced Gearing	Gearing level now below 42%
Strengthened management team	Driving significant change and improvement across the business
ADP	Re-establishment of ADP operations still on track to commence in 2HY2013
Strong manufacturing	Contract manufacturing grew 4% for the year with material further growth forecast for FY13

Continued reduction in gearing



Growth in contract manufacturing ($,000)



STRATEGIC REVIEW PROGRESS

EUROPE

Discontinued a range of non-core and underperforming brands

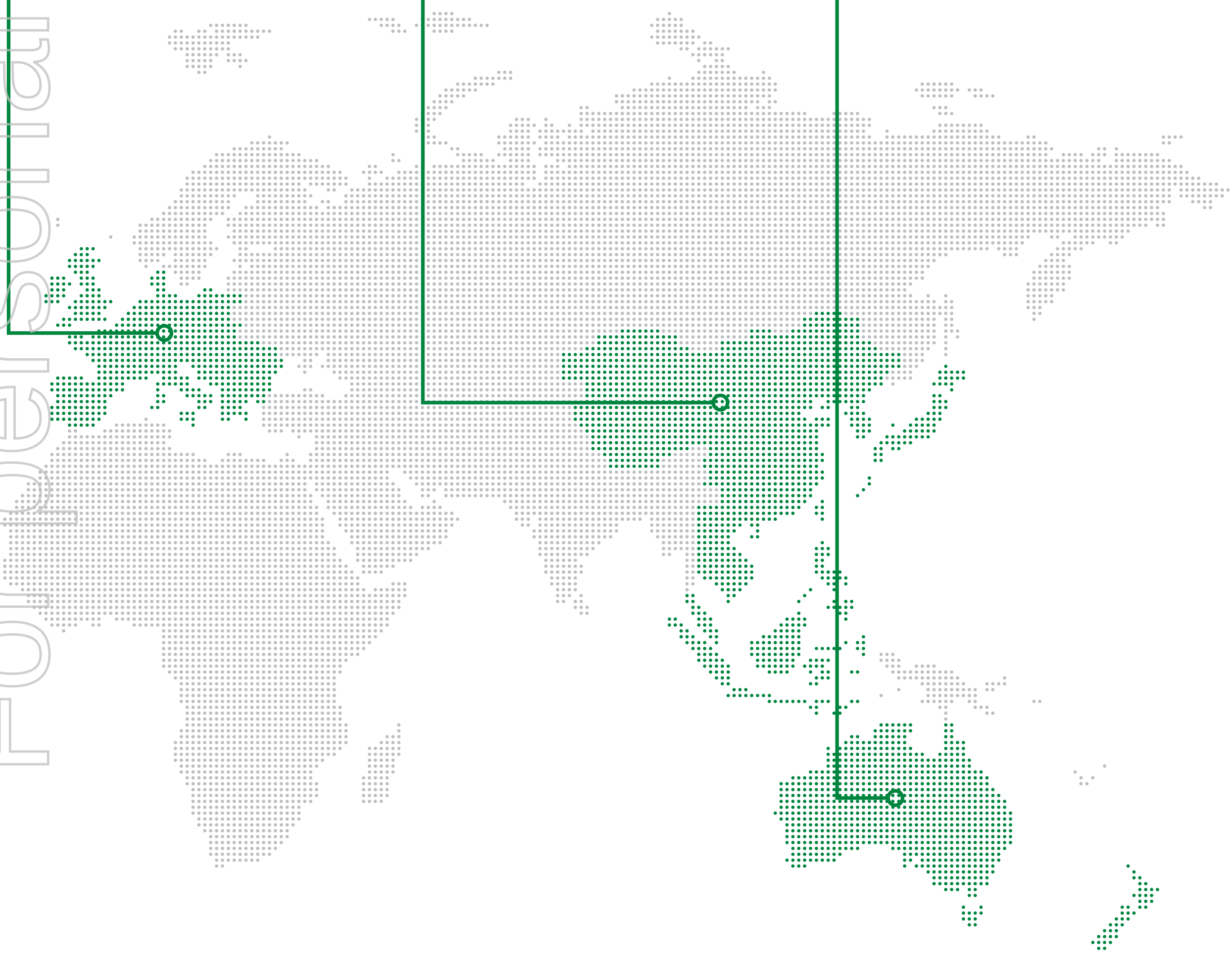
ASIA

Fully divested China and Hong Kong operations and entities

AUSTRALIA

Closed and sold Bundaberg (QLD) production facility.

Sold the Milton brand, including all intellectual property and business assets



THE FUTURE

"Following several tough years, the company is showing good signs of turning around its financial performance for the better, and it has a very confident view about the immediate future outlook for the business"

KEY OPPORTUNITIES AND BUSINESS INITIATIVES FOR THE COMING YEAR

- Open distribution of the Group's flagship weight management range, Celebrity Slim: Since its launch in 2007, Celebrity Slim has been sold exclusively in Priceline stores. In FY2013, CELEBRITY SLIM has now been made available to the open market, with significant ranging now obtained in Woolworths & Coles (all stores), Target (all stores), leading pharmacy groups, continued ranging in all Priceline stores and other select grocery and variety retail groups. This open distribution is resulting in a significant increase in demand for its weight loss products, and the board is confident of this area of the business delivering an improved financial performance in FY2013.
- Re-establishment of ADP Plant: Once completed, the ADP protein plant is forecast to deliver strong cash flow and earnings to the Group as well as driving our long term product development pipeline. This project is scheduled to be completed and operational in the middle of the second half of FY13.
- Growth in Europe: The Group has now obtained a significant increase in the distribution of its Celebrity Slim range in the United Kingdom and this is forecast to deliver a significant increase in the sales revenue of this business unit in the coming year.
- Intellectual Property development: The Group continues to progress the development of its intellectual property pipeline with the release of three new pharmaceutical products with a further two products now registered and ready for imminent launch. The Group has an additional six pharmaceutical products expected to be lodged for approval by the TGA during FY2013, with additional products under development. The Directors believe that this pipeline of innovative new products will assist the Group in securing future growth under its own brands along with contract manufacturing and out licensing opportunities.
- Growth in pharmaceutical manufacturing: As intimated earlier in this report, the Group has experienced a significant increase in demand for its contract manufacturing services, which is forecast to provide a material increase in the revenue of this division in FY13. In addition to this, the Group's pharmaceutical ranges are forecast to continue to grow during FY13 .

Construction of ADP site in progress

Financials

CORPORATE GOVERNANCE

1. Probiotec's approach to corporate governance

Overview

The Board is committed to maintaining a high standard of corporate governance. The Board believes that its corporate governance values and behaviours underpin the company's everyday activities to ensure transparency, fair dealing and protection of the interests of stakeholders. Consistent with this belief, the Board's approach is to consider corporate governance within the broader framework of corporate responsibility and regulatory oversight.

In pursuing its commitment to best practice governance standards, the Board will continue to:

- review and improve its governance practices; and
- monitor developments in best practice corporate governance.

In Australia, we have examined the 'Principles of Good Corporate Governance and Best Practice Recommendations' first published in March 2003, the second edition published in August 2007 and the 2010 amendments published in June 2010 by the Australian Securities Exchange's Corporate Governance Council, the Commonwealth Government's CLERP 9 legislation and the Australian Standard AS8000 Good Governance Principles. We have analysed these developments and adapted practices where appropriate to ensure Probiotec remains at the forefront in protecting stakeholder interests.

The Board's approach has been to be guided by the principles and practices that are in our stakeholders' best interests while ensuring full compliance with legal requirements.

Compliance with the ASX best practice recommendations

Probiotec considers its governance practices comply with all ASX best practice recommendations. As required by the ASX best practice recommendations, Probiotec has copies of each corporate governance practice described below on its website at www.probiotec.com.au.

Probiotec also publishes on its website the annual reports, profit announcements, CEO and executive briefings, economic updates, notices of meeting, media releases and meeting transcripts.

2. Date of this statement

This statement reflects our corporate governance policies and procedures as at 30 September 2012.

3. The Board of Directors

Membership and expertise of the Board

The Board has a broad range of relevant financial and other skills, experience and expertise to meet its objectives. The current Board composition, with details of individual Director's backgrounds, is set out in the attached Directors report.

Board role and responsibility

The Board is accountable to shareholders for Probiotec's performance. The Board has formalised its roles and responsibilities into a Charter, which defines the matters that are reserved for the Board and those that the Board has delegated to management.

In summary, the Board's responsibilities include:

- providing strategic direction and approving corporate strategic initiatives;
- selecting and evaluating future Directors, the Chief Executive Officer ('CEO') and the Chief Financial Officer ('CFO');
- planning for Board and executive succession;
- setting CEO and Director remuneration within shareholder approved limits;
- approving Probiotec's budget and monitoring management and financial performance;
- considering and approving Probiotec's Annual Financial Report and the interim and final financial statements;
- approving Probiotec's risk management strategy, monitoring its effectiveness and maintaining a direct and ongoing dialogue with Probiotec's auditors and regulators; and
- considering and reviewing the social and ethical impact of Probiotec's activities, setting standards for social and ethical practices and monitoring compliance with Probiotec's social responsibility policies and practices.

The Board has delegated to management responsibility for:

- developing and implementing corporate strategies
- making recommendations on significant corporate strategic initiatives;
- maintaining an effective risk management framework and keeping the Board and market fully informed about material risks;
- developing Probiotec's annual budget, recommending it to the Board for approval and managing day-to-day operations within the budget and in accordance with standards for social and ethical practices which have been set by the Board; and
- making recommendations for the appointment of senior management, determining terms of appointment, evaluating performance, and developing and maintaining succession plans for senior management roles.

CORPORATE GOVERNANCE (continued)

Board size and composition

The Board determines its size and composition, subject to the limits imposed by Probiotec's Constitution, a copy of which is available on Probiotec's website. The Constitution requires a minimum of three and a maximum of seven Directors. At the date of this report, there are four Non-executive Directors and two Executive Director on the Board.

The selection and role of the Chairman

The Chairman is selected by the Board.

The current Chairman, Maurice Van Ryn, is a Non-executive independent Director appointed by the Board. He has been a Director and Chairman of Probiotec since July 2006. The Chairman is a member of the Audit and Risk Committee.

Directors' independence

The Board assesses each of the Directors against specific criteria to decide whether they are in a position to exercise independent judgement.

Directors are considered to be independent if they are independent of management and free from any business or other relationship that could materially interfere with, or could reasonably be perceived to materially interfere with, the exercise of their unfettered and independent judgement. Materiality is assessed on a case-by-case basis by reference to each Director's individual circumstances rather than general materiality thresholds.

In assessing independence, the Board considers whether the Director has a business or other relationship with Probiotec, directly or as a partner, shareholder or officer of a company or other entity that has an interest, or a business or other relationship, with Probiotec or another Probiotec group member.

It is the Board's view that each of its Non-executive Directors, Maurice Van Ryn, Graham Buckeridge, Robert (Max) Johnston and Richard Kuo is independent.

Meetings of the Board and their conduct

The Board meets formally approximately twelve times a year. In addition, it meets whenever necessary to deal with specific matters needing attention between the scheduled meetings. The Chairman and the CEO establish meeting agendas to ensure adequate coverage of financial, strategic and major risk areas throughout the year. In addition to its formal meetings, the Board may also undertake relevant workshops.

These meetings will include workshops on executive and senior management succession planning, corporate governance, Probiotec's risk/reward approach, customer experience and segmentation projects and other major strategic initiatives.

Directors are always encouraged to participate with a robust exchange of views and to bring their independent judgements to bear on the issues and decisions at hand.

Executive management regularly attends Board meetings and are also available to be contacted by Directors between meetings. The Board also meets without executive management (other than the CEO and any Executive Directors) at each meeting. The Board meets without the CEO and any Executive Directors once a year or as required.

Review of Board performance

The Board regularly reviews its overall performance, as well as the performance of Committees, individual Directors and executive management. The performance of Non-executive Directors (including the Chairman) is subject to annual peer and executive management review. The process can include written surveys of Directors, the Company Secretary and a selection of Group Executives. The survey results are independently collated and the Chairman formally discusses the results with individual Directors and Committee chairs.

Retirement and re-election of Directors

Probiotec's Constitution states that one-third of our Directors must retire each year. A Director will hold office until such time as they vacate the office or are removed under the Constitution. The Constitution also states that any Director who has been appointed during the year must retire at the next annual general meeting. Eligible Directors who retire each year may offer themselves for re-election by shareholders at the next annual general meeting.

The Board Nomination and Remuneration Committee evaluates the contribution of retiring Directors prior to the Board endorsing their candidature.

Board access to information and advice

All Directors have unrestricted access to company records and information and receive regular detailed financial and operational reports from executive management to enable them to carry out their duties. The Board collectively, and each Director individually, has the right to seek independent professional advice at Probiotec's expense to help them carry out their responsibilities. While the Chairman's prior approval is needed, it may not be unreasonably withheld and, in its absence, Board approval may be sought.

4. Board committees

Board committees and membership

There are currently two Board Committees whose powers and procedures are governed by Probiotec's Constitution and the relevant Committee's Charters, as approved by the Board.

The two Board Committees and their membership are set out below:

- Audit and Risk Management Committee
- Nomination and Remuneration Committee

Other separate Committees, such as the Corporate Social Responsibility Committee, may be established from time to time to consider matters of special importance.

Committee Charters

The roles and responsibilities of each Committee are set out in the Committee Charters.

Committee procedures

Operation of the Committees and reporting to the Board

The Board Committees meet twice yearly in conjunction with the release of financial results or more frequently as circumstances dictate. Each Committee is entitled to the resources and information it requires, including direct access to employees and advisers. The CEO, senior executives and other employees are invited to attend Committee meetings. All Directors receive all Committee papers and can attend all Committee meetings.

Composition and independence of the Committees

Committee members are chosen for the skills, experience and other qualities they bring to the Committees. All committees are currently composed of a majority of independent Non-executive Directors.

How the Committees report to the Board

As soon as possible following each Committee meeting, the Board is given a verbal report by each Committee Chair and all Committee minutes are tabled at Board meetings.

How Committees' performance is evaluated

The performance of Committees is discussed and reviewed initially within each Committee and then reviewed as part of the Board's performance review. The performance of each member of the Committees is evaluated as part of the performance review of each Director.

Board Audit and Risk Management Committee

Role of the Committee

The Board Audit and Risk Management Committee (ARM) will:

- be the focal point of the communication between the Board, management and the external auditor;
- recommend and supervise the engagement of the external auditor and monitor auditor performance;
- review the effectiveness of management information and other systems of internal control;
- review all areas of significant credit, market, operational and compliance risk and arrangements in place to contain those to acceptable levels;
- review significant transactions that are not a normal part of the Company's business;
- review the year end and interim financial information and ASX reporting statements;
- monitor the internal controls and accounting compliance with the Corporations Act, ASX Listing Rules, review external audit reports and ensure prompt remedial action;
- review the Company's financial statements (including interim reports) and accounting procedures; and
- review and approve the framework for the management of operational risks including compliance with the provisions of the Therapeutic Goods Administration Act (TGA), requirement of the Australian Quarantine Inspection Service (AQIS) and other relevant legislation.

Integrity of the financial statements

ARM considers whether the accounting methods applied by management are consistent and comply with accounting standards and concepts. ARM reviews and assesses any significant estimates and judgements in financial reports and monitors the methods used to account for unusual transactions.

In addition it assesses the processes used to monitor and ensure compliance with laws, regulations and other requirements relating to external reporting of financial and non-financial information.

External audit

ARM is responsible for making recommendations to the Board concerning the appointment of our external auditors and the terms of their engagement. ARM reviews the performance of the external auditors and annually reviews policy on maintaining independence of the external auditor. The independent external auditor reports directly to ARM and the Board. ARM meets with the external auditor in the absence of management with ARM members being able to contact the external auditor directly at any time.

CORPORATE GOVERNANCE (continued)

Operational Risk

ARM reviews the appropriateness of the framework adopted for managing operational risk and reviews operational risk issues and action plans to address control improvement areas.

Compliance with legal and regulatory requirements

ARM ensures conformity with applicable legal and regulatory requirements and the Code of Conduct. ARM also establishes procedures for the receipt, retention and treatment of complaints, including accounting, internal accounting controls or auditing matters and the confidential, anonymous submission by employees of concerns regarding accounting or auditing matters.

ARM also discusses with management and the external auditor correspondence with regulators or government agencies and published reports which raise material issues. ARM discusses with the Quality Control Manager matters that may have a material impact on product regulatory compliance and with the Company Secretary matters that have a material impact on the financial statements or the compliance with reporting and disclosure policies. The General Manager - Quality reports directly to the Chairman on matters covered by the Therapeutic Goods Administration Act (TGA) and the Australian Quarantine Inspection Service (AQIS) and forwards copies of all matters covered under either TGA or AQIS reports to the chair of ARM.

Composition of ARM

ARM membership is three Non-executive, independent Directors who possess an understanding of the industry in which Probiotec operates: Richard Kuo (Chairman) (who is financially literate), Graham Buckeridge (who has financial expertise) and Maurice Van Ryn (who has financial expertise).

Board Nomination and Remuneration Committee

Role of the Committee

The Board Nomination and Remuneration Committee (NRC) develops and reviews policies on:

- Director tenure;
- Board composition, strategic function and size;
- eligibility criteria for nominating Directors;
- the effectiveness of the Board and Board committees;
- makes recommendations to the Board on the CEO's remuneration;
- approves the reward levels for our senior management group;
- approves merit recognition arrangements and long and short term incentive arrangements; &
- makes recommendations to the Board on Directors' fees.

NRC periodically reviews our criteria for appointing Directors and considers and recommends to the Board Directors who are retiring by rotation, candidates to be nominated as Directors and reviews periodically the process for orientation and education of new Directors.

The CEO determines the remuneration packages for the senior executives of the Company in accordance with compensation guidelines set by the Board. The Board remuneration policy has been developed to ensure that remuneration packages properly reflect each person's duties and responsibilities and that remuneration is competitive in attracting, retaining and motivating people of the highest quality.

NRC may engage independent remuneration consultants to ensure that our pay and reward practices are consistent with the market practice.

Composition of NRC

NRC membership is: Robert (Max) Johnston (Chairman), Graham Buckeridge and Wayne Stringer.

Board Corporate Social Responsibility Committee

Role of the Committee

A separate Board Corporate Social Responsibility Committee (CSR) has not been formed. These matters are considered by the Board who review the social and ethical impacts of our policies and practices and to oversee initiatives to enhance Probiotec's reputation as a socially responsible corporate citizen. CSR matters are monitored for compliance with Probiotec's published social responsibility policies and practices to ensure Probiotec meets its obligations to its stakeholders. Details of Probiotec's corporate responsibility objectives are addressed in section 8.

5. Audit governance and independence

Approach to audit governance

Best practice in financial and audit governance is changing rapidly. The Board is committed to three basic principles:

- Probiotec must produce true and fair financial reports;
- its accounting methods are comprehensive and relevant and comply with applicable accounting rules and policies; and
- the external auditors are independent and serve shareholder interests by ensuring that shareholders know Probiotec's true financial position.

Engagement and rotation of external auditor

Probiotec's independent external auditor is Moore Stephens (MS). MS were appointed in 2012 in accordance with the provisions of the Corporations Act.

The Board has adopted a policy that the lead signing and review audit partners' responsibilities can be performed by the same person for no longer than 5 years. The present lead MS partner for Probiotec's audit is Nick Michael. The Board also requires a minimum five-year 'cooling off' period before an audit partner is allowed back onto the audit team.

Certification and discussions with external auditor on independence

The Board Audit and Risk Management Committee (ARM) requires the external auditor to confirm that they have maintained their independence.

Probiotec's external auditor gives annual assurance to ARM and to the Board that they have complied with the independence standards, promulgated by regulators and professional bodies. Periodically ARM meets separately with the external auditor.

Relationship with external auditor

Probiotec's current policies on employment and other relationships with our external auditor are:

- the audit partners and any audit firm employee on the Probiotec audit are prohibited from being an officer of Probiotec;
- an immediate family member of an audit partner or any audit firm employee on the Probiotec audit is prohibited from being a Director or an officer in a significant position at Probiotec;
- a former audit firm partner or employee on the Probiotec audit is prohibited from becoming a Director or officer in a significant position at Probiotec for at least five years and after the five years, can have no continuing financial relationship with the audit firm;
- members of the audit team and firm are prohibited from having a business relationship with Probiotec or any officer of Probiotec unless the relationship is clearly insignificant to both parties;
- the audit firm, its partners, its employees on the Probiotec audit and their immediate family members are prohibited from having loans or guarantees with Probiotec;
- the audit firm, its partners, its employees on the Probiotec audit and their immediate family members are prohibited from having a direct or material indirect investment in Probiotec;
- officers of Probiotec are prohibited from receiving any remuneration from the audit firm;
- the audit firm is prohibited from having a financial interest in any entity with a controlling interest in Probiotec; and
- the audit firm engagement team in any given year cannot include a person who had been an officer of Probiotec during that year.

Restrictions on non-audit services by the external auditor

The external auditor is not able to carry out the following types of non-audit services for Probiotec:

- preparation of accounting records;
- information technology systems design and implementation;
- valuation services and other corporate finance activities;
- internal audit services;
- temporary senior staff assignments or management functions;
- legal services;
- litigation services;
- actuarial services; and
- recruitment services for senior management.

For all other non-audit services, use of the external audit firm must be assessed in accordance with Probiotec's policy requiring an independence assessment be done by the business manager requiring the service. The approval of the ARM Chairman must also be obtained.

Attendance at Annual General Meeting

Probiotec's external auditor attends the annual general meeting and is available to answer shareholder questions.

6. Controlling and managing risk

Approach to risk management

Taking and managing risk are central to business and to building shareholder value. Probiotec's approach is to identify, assess and control the risks which affect its business. This enables the risks to be balanced against appropriate rewards for the taking and managing of the risks. The risk management approach links Probiotec's vision and values, objectives and strategies, and procedures and training.

Probiotec recognises three main types of risk:

- credit risk, being the risk of financial loss from the failure of customers to honour fully the terms of their contract;
- market risk, being the risk to earnings from changes in market factors such as interest and foreign exchange rates, or our liquidity and funding profiles; and
- operational and compliance risk, which arises from inadequate or failed internal processes, people and systems or from external events and include compliance with regulations that govern Probiotec's work practices and information technology.

These risk categories are interlinked and therefore we attempt to take an integrated approach to managing them through the work of the Board Audit and Risk Management Committee (ARM) including copies of all TGA reports issued by the General Manager – Quality to the Chairman.

Risk management roles and responsibilities

ARM is responsible for approving and reviewing Probiotec's risk management strategy and policy. Executive management is responsible for implementing ARM-approved risk management strategy and developing policies, controls, processes and procedures to identify and manage risks in all of Probiotec's activities.

CEO and CFO assurance

The Board receives regular reports about the financial condition and operational results of Probiotec and its controlled entities.

The CEO and the CFO periodically provide formal statements to the Board that in all material respects:

- the company's financial statements present a true and fair view of Probiotec's financial condition and operational results, and
- the risk management and internal compliance and control systems are sound, appropriate and operating efficiently and effectively.

7. Remuneration framework

Overview

Probiotec has a robust framework in place to ensure that the level and composition of remuneration is sufficient and reasonable and linked to performance. Details of framework and policies and practices are set out in the Directors' Report including a description of the broad structure and objectives of the remuneration philosophy and the measures used to continually link reward to performance.

Non-executive Directors

Non-executive Directors' fees and payments are reviewed annually by the Board. The Board may access the advice of independent remuneration consultants to ensure Non-executive Directors' fees and payments are appropriate and in line with the market.

Executives

The objective of Probiotec's executive reward framework is to ensure reward for performance is competitive and appropriate for the results delivered. The framework is designed to follow best practice for the alignment of executive reward with shareholder value as measured by economic profit.

Equity-related reward and performance plans overview

All equity-related reward and performance plans are reviewed and assessed by the Board Nomination and Remuneration Committee before being considered and approved by the Board.

8. Corporate social responsibility

Approach to corporate social responsibility

Probiotec's aim is to manage its business in a way that produces positive outcomes for all stakeholders and maximises economic, social and environmental value simultaneously. In doing so, Probiotec accepts that the responsibilities flowing from this go beyond both strict legal obligations and just the financial bottom line.

Transparency, the desire for fair dealing, responsible treatment of staff and of customers, and positive links into the community underpin our everyday activities and corporate social responsibility practices.

Probiotec's approach reflects the many legal, regulatory and prudential requirements applying to our industry.

Probiotec's Code of Conduct and responsibility codes

Probiotec's Code of Conduct applies to all Directors, executives, management and employees without exception. The Code governs workplace and human resource practices, risk management and legal compliance and is reviewed periodically and has been specifically reviewed to reflect the ASX best practice recommendations.

Beyond the Code of Conduct, Probiotec has a series of further responsibility policies and codes including:

- Securities Trading policy;
- Market Disclosure policy;
- Whistleblower Protection policy;
- Diversity policy; and
- Corporate Social Responsibility policy.

Compliance policy and practices

Probiotec's compliance approach focuses on: ensuring strict adherence to all laws and regulations; maintaining the quality control of practices and processes; identifying any weaknesses; and moving to fix any gaps while enhancing the processes and practices.

A separate compliance governance framework operates involving the Board Audit and Risk Management Committee (ARM), to the General Manager - Quality and Company Secretary (who both report regularly to ARM), and individual line businesses. The prime responsibility for compliance resides with line management, who are required to demonstrate that they have effective processes in place consistent with Probiotec's compliance principles and practices.

Concern reporting and whistle blowing

Employees are actively encouraged to bring any problems to the attention of management or the Board, including activities or behaviour which may not be in accord with the Code of Conduct, Securities Trading Policy, other Probiotec policies, or other regulatory requirements or laws.

Concerns can be raised directly with senior management through the concern raising process, including the CEO and CFO's intranet site or via the CEO's telephone hotline. Concerns can also be raised anonymously by phone and online through the concern reporting system, and are directed to the General Manager - Quality in relation to products and operational matters, and to the Company Secretary in relation to financial matters. This concern reporting system protects individuals who, in good faith, report any apparent or actual violations of our codes. The concern reporting system is being reviewed against the Australian standard AS 8004 (Whistleblower protection programs).

Securities trading policy

Directors and employees are subject to restrictions under the law relating to dealing in Probiotec's securities if they are in possession of inside information. Inside information is information that is not generally available and, if it were generally available, a reasonable person would expect it to have a material effect on the price or value of the securities of the company. In addition and subject always to the above legal restrictions, Probiotec has policies in place which restrict the dates when Directors (and employees who have access to inside information) can deal in Probiotec's securities.

The key aspects of the policy are:

- Trading whilst in the possession of price sensitive information is prohibited.
- Trading is permitted without approval in the 6 week period after the release to the ASX of the half-yearly and annual results, the end of the AGM or at any time the Company has a prospectus open, but only if they have no inside information and the trading is not for short term or speculative gain.
- Trading in other circumstances is only permitted if the person is personally satisfied that they are not in possession of inside information and they have obtained the requisite approval. Permission will be given for such trading only if the approving person is satisfied that the transaction would not be contrary to law, for speculative gain or to take advantage of inside information.

Diversity policy

The Board adopted a diversity policy in September 2012.

Probiotec aims to provide an environment in which all employees have equal access to opportunities at work, whilst upholding the principle of meritocracy at all times.

Probiotec believes that fostering diversity at all levels allows the Group to provide greater alignment to customer needs, improves the creativity and innovation of leadership teams, and supports the development of an enhanced talent pipeline for key and future roles by enabling access to a broader pool of talent.

Probiotec strives to create a work environment free of discrimination and harassment, regardless of their gender, age, race, disability, sexual orientation, cultural background, religion, family responsibilities or any other area of potential difference.

The key objectives of the policy are:

- Foster an inclusive culture;
- Improve talent management;
- Enhance recruitment practices; and
- Ensure pay equity.

As at 30 June 2012, the Probiotec Group had the following female participation (%) rates:

Probiotec Limited non-executive directors	0
Senior executive positions	25
Other management and professional roles	44
Total workforce	42

Market disclosure policy and practices

Probiotec is committed to giving all shareholders equal access to material information about our activities, and to fulfil continuous disclosure obligations to the broader market.

The Board-approved market disclosure policy governs how Probiotec communicates with shareholders and the market.

This policy is designed to ensure compliance with ASX Listing Rules continuous disclosure requirements so as to ensure any information that a reasonable person would expect to have a material effect on the price of Probiotec's securities is disclosed.

The CEO is responsible for making decisions on what should be disclosed publicly under the market disclosure policy, and for developing and maintaining relevant guidelines, including guidelines on information that may be price sensitive.

The Company Secretary has responsibility for ensuring compliance with the continuous disclosure requirements in the ASX Listing Rules, and overseeing and coordinating information disclosure to the ASX, analysts, brokers, shareholders, the media and the public.

DIRECTOR'S REPORT

The directors submit the financial report of Probiotec Limited and its controlled entities ("the Group") for the financial year ended 30 June 2012.

Directors

The names of the directors in office at any time during or since the end of the year are:

Maurice Van Ryn	*Non-Executive Chairman*
Charles Wayne Stringer	*Executive Director*
Wesley Stringer	*Executive Director*
Graham Harry Buckeridge	*Non-Executive Director*
Richard David Kuo	*Non-Executive Director*
Robert Maxwell Johnston	*Non-Executive Director*

Directors have been in office to the date of this report unless otherwise stated.

Company Secretary

The name of the company secretary in office at any time during or since the end of the year was:

Jared Stringer

The company secretary has been in office to the date of this report unless otherwise stated.

Principal Activities

The Group's principal activities in the course of the financial year were the development, manufacture and sale of pharmaceuticals, foods and nutraceutical products in Australian and international markets.

Operating Results

The consolidated profit of the Group attributable to the shareholders for the financial year was $1,249,380 (2010: loss of $10,337,786).

Dividends

No dividend has been declared or paid in regards to the financial year ended 30 June 2012 (2011: $nil).

Review of operations

For the year ended 30 June 2012, the Group generated sales revenue of $66,464,509, a decline of 9.6% on the previous financial year. Sales revenue was most significantly impacted by the discontinuance of a number of non-core and loss making operations, together with a continued decline in sales of the Group's meal replacement weight loss ranges. The Group's net profit attributable to members for the financial year (excluding non-cash impairment costs) was $2,627,573, compared to the previous financial year loss of ($4,522,280). At a statutory reported level, the Group's net profit attributable to members for the financial year was $1,249,380, a material reversal over the previous financial year's loss of ($10,337,786).

The Group's statutory net profit attributable to members for the financial year of $1,249,380 was both positively and negatively impacted by a range of adjustments made following the strategic review of the Group announced last financial year. This strategic review resulted in a range of initiatives being implemented to improve the strategic focus, business operations and the financial performance of the Group.Full details of the initiatives (and their impact on the financial performance of the Group) can be found below and in Note 6 of the financial report of the Group for the year ended 30 June 2012.

The combination of an improvement in working capital levels together with the financial benefits flowing from the implementation of the strategic initiatives (most notably, the sale of the Milton brand) has resulted in a material reduction in the Group's debt.

For the year ended 30 June 2012, the Group generated $4,730,105 in free cash flow (being cash flow from operating activities plus cash flow from investing activities), an increase of 63.5% over the prior corresponding period. Total interest bearing liabilities, net of cash, as at 30 June 2012 was $ 23,636,014, a decrease of 16.7% from the same date in the previous year. The Group's gearing ratio, as at 30 June 2012 was 41.2%, down from 45.7% at the balance date last year (see Note 24(a) for further details).

This result shows what the directors believe to be the beginning of a sustained improvement in the performance of the Group as the full benefits of the strategic initiatives being undertaken, along with a strengthened management team, are obtained. Most pleasingly, despite the difficult economic conditions (highlighted by continued weakness in the retail environment), the Group has made a return to profitability in its underlying business.

Progress on strategic review initiatives

During the year, the Group has completed the majority of the initiatives identified in the strategic review announced in June 2011. Most notably, the Group has:

- fully divested its China and Hong Kong operations and entities (see note 6 of the financial report);
- discontinued a range of non-core and underperforming brands (see note 6 of the financial report);
- closed and sold its Bundaberg (QLD) production facility (see note 17 of the financial report); and
- sold the Milton brand, including all intellectual property and business assets (see note 18 of the financial report).

These initiatives resulted in a range of adjustments to the financial statements for the year ended 30 June 2012, including non-cash impairment expenses of $1.4 million being incurred along with a profit after tax on the sale of the Milton brand of $1.8 million. These impairment expenses related to the impairment of intangibles, investments and other current assets associated with discontinued operations and brands.

These completed initiatives are now expected to provide significant improvements in the Group's ability to generate attractive earnings and cash flow from its ongoing operations.

Review of ongoing operational segments

Sales in the Group's pharmaceutical and consumer health segment, comprising our traditional pharmaceutical ranges (including Gold Cross, David Craig, Lomotil and Vermox), weight loss and sport nutrition products fell by 6.8 % over the previous year to $35,706,162. The difficult economic conditions in the domestic retail environment continued to impact the sales of the Group's products, most notably in the Group's weight loss ranges. As a consequence of softening sales in the weight loss products, the Group defined and implemented a revised open sales and distribution model, as opposed to the exclusive and closed arrangement that applied to many of its products. As a consequence and notably, the Group is experiencing a significant increase in demand in this segment, including its weight loss products, and is confident of delivering an improved financial performance in FY2013.

The Group continues to progress the development of its intellectual property pipeline with the release of three new pharmaceutical products with a further two products now registered and ready for imminent launch. The Group has an additional six pharmaceutical products expected to be lodged for approval by the TGA during FY2013, with additional products under development. The Directors believe that this pipeline of innovative new products will assist the Group in securing future growth under its own brands along with contract manufacturing and out licensing opportunities.

The Group's contract manufacturing segment continued to experience solid demand, with a greater level of focus and resources allocated to this segment. Sales revenue from contract manufacturing was $17,514,134, an increase of 4.4% over the prior corresponding period. Encouragingly, the Group is continuing to experience strong demand in contract manufacturing and has a growing order book for the 2013 financial year and expects this segment to achieve continued growth over the 2012 financial year. The majority of contract manufacturing activity was on behalf of major pharmaceutical companies.

As a result of the strategic initiatives detailed above, the Group has restructured and refocused its export activities. The Group is now focusing primarily on its manufacturing and distribution businesses in the United Kingdom and Ireland. Export sales revenue fell 21.9% from the prior year to $8,760,539, however as a result of the rationalisation and/or closure of a number of loss making countries / entities these activities are now profitable. This improvement in profitability was achieved despite the continued significant strengthening of the Australian dollar against both the Euro and Great Britain pound. The Group has now obtained a significant increase in the distribution of its Celebrity Slim range in the United Kingdom (set to commence sale from September 2012) and this is forecast to deliver a significant increase in the sales revenue of this segment in the coming year.

Sales in the nutritional products segment declined 37.6% on the prior corresponding period to $4,484,168. This decline was primarily a result of the closure of the Group's Queensland facility and the rationalisation of underperforming product ranges, as a consequence of the strategic initiatives being implemented.

ADP Project update

During the year, the Group entered into an agreement with United Dairy Power Pty Ltd (UDP) to relocate its protein fractionation plant (ADP Plant) and recommence production of whey derived pharmaceutical grade dairy proteins through its Australian Dairy Protein subsidiary (ADP). In accordance with the terms of this agreement, the Group is progressing the relocation of its ADP Plant to UDP's Jervois processing site in South Australia.

The ADP Plant will produce the dairy protein fraction Lactoferrin along with the world's only dairy based high purity Immunoglobulins. The Group proposes to sell both Lactoferrin and Immunoglobulins into the infant nutrition, human nutrition and pharmaceuticals markets, as well as continuing to research and develop a range of exciting pharmaceutical applications. Commencement of production is expected in the middle of the second half of the current financial year.

Significant Changes in State of Affairs

Significant changes in the state of affairs of the Group comprised the continued implementation of the Group's strategic review and associated activities as outlined in the review of operations and expanded upon in note 6 of the financial report for the year ended 30 June 2012.

There was no other significant change in the state of affairs of the Group other than that referred to in the financial statements or notes thereto and elsewhere in the financial report of the company and its controlled entities for the year ended 30 June 2012.

Significant After Reporting Date Events

There has not been any matter or circumstance, other than that referred to in the financial statements or notes thereto, that has arisen since the end of the financial year, that has significantly affected, or may significantly affect, the operations of the Group, the results of those operations, or the state of affairs of the Group in future financial years.

Future Developments

The Group will continue to operate its business consistent with its stated business strategy of growing both its pharmaceutical and nutritional/nutraceutical business segments. The Board will continue to monitor the progress of the business improvement initiatives and the intended improvement in the Group's operating and financial performance. Should further decisions and actions become necessary, then these will be made and within the framework of growing both profitability and cash flow of the Group.

Environmental Issues

The Group monitors its environmental legal obligations and has its own self imposed policies. We believe that the Group complies with all aspects of the environmental laws.

Occupational Health and Safety

The Group's Occupational Health and Safety Committee meet monthly and monitors the business by conducting regular audits of the premises. Any safety matters raised either by staff, the audits or from an investigation of any workers' compensation claims are reviewed and, where appropriate, changes made to operating procedures. Staff are encouraged to make safety suggestions to their departmental representatives. All committee members are given the necessary training for the position.

Directors' Benefits

No director has received or become entitled to receive a benefit other than directors' remuneration. Full details of the level of remuneration received by Directors can be found in the Remuneration Report on page 21 of the Directors Report.

Meetings of Directors

Probiotec Limited became a public company on 17th February 2006 and listed on the Australian Stock Exchange on the 14th November 2006. Directors hold meetings every month. The board also comprises the Audit and Risk Management and Remuneration and Nominations Sub-Committees. The number of meetings of the company's board of directors held during the year ended 30 June 2012, and the numbers of meetings attended by each director were:

	Board of Directors Meetings		Audit & Risk Management Committee meetings		Remuneration & Nominations Committee meetings	
Director	**No. Held***	**No. Attended**	**No. Held****	**No. Attended**	**No. Held****	**No. Attended**
Maurice Van Ryn	11	11	3	3	-	-
Charles Wayne Stringer	11	11	-	-	2	2
Graham Harry Buckeridge	11	10	3	3	2	2
Richard David Kuo	11	10	3	3	-	-
Wesley Stringer	11	9	-	-	-	-
Robert Maxwell Johnston	11	10	-	-	2	1

** Number of board meetings held while director eligible to attend.* *** Number of meetings for members of respective board or committee only.*

Information on Directors and Officers

Maurice Van Ryn

Role	- Chairman (Non-executive)
Qualifications	- Bachelor of Business (RMIT)
Experience	- Appointed Chairman in July 2006. Previously held the position of CEO of Bega Cheese and is currently Bega Cheese's Manager Consumer Products - International. Maurice has 32 years experience in direct management of food companies in the Australian manufacturing sector.
Special Responsibilities	- Member of Audit and Risk Committee.
Other Directorships	- Non-executive Director of Medical Development International Limited (since October 2003).

Graham Harry Buckeridge

Role	- Non-Executive Director
Qualifications	- Dip Bus, CPA, FFIN
Experience	- Co-founder and executive director of BG Capital Corp Ltd (BGC) a relationship based firm providing corporate advisory and investment banking services. Previously joint founder and Managing Director of Burdett Buckeridge and Young, a member corporation of ASX. Graham has extensive experience in all aspects of international and domestic financial markets.
Special Responsibilities	- Member of Remuneration and Nominations Committee.
Other Directorships	- Executive Director of BG Capital Corp Limited Executive Chairman of Abacus Film Fund

Richard David Kuo

Role	- Non-Executive Director
Qualifications	- B.Com, LLB, MAICD
Experience	- Holds Commerce and Law degrees with post graduate qualifications in applied finance and investment. Brings with him 26 years experience in law, investment banking and corporate strategy. Currently manages Pier Capital, a privately owned investment banking firm which provides corporate advice to a broad range of corporations and has extensive experience in mergers and acquisitions, capital markets and strategic planning.
Special Responsibilities	- Responsibilities include Chairman of the Audit and Risk Management Committee.
Other Directorships	- Non-Executive Director of Glenorchy Art and Sculpture Park Limited

Robert Maxwell Johnston

Role	- Non-Executive Director
Qualifications	- FCDA, MAICD
Experience	- A former senior executive with Johnson & Johnson, the world's largest Medical, Pharmaceutical and Consumer Healthcare company. Mr. Johnston was president and CEO of Johnson & Johnson Pacific, while also concurrently leading several Asia Pacific Franchise and Functional working group. Brings extensive overseas experience during his career in leading businesses in both Western and Central-Eastern Europe and Africa. Prior to joining Johnston & Johnson, Max's career also included senior roles with Diageo and Unilever.
Special Responsibilities	- Chairman of Remuneration and Nominations Committee.
Other Directorships	- Non-Executive Director of Enero Group Limited

DIRECTOR'S REPORT (continued)

Charles Wayne Stringer

Role	- Chief Executive Officer (Executive Director)
Qualifications	- Dip. Bus, ACA
Experience	- CEO of Probiotec since it was founded in 1997. Overseen the development of a series of joint ventures and commercial opportunities and acquisition of Pharmaction in the 2004 financial year and the Biotech Milton Pharmaceutical company in 2005. Wayne also spent several years as a CEO and director of companies involved in manufacturing, retailing, finance, mining and waste management.
Special Responsibilities	- Responsibilities include strategic management, remuneration and operational oversight.
Other Directorships	- Nil

Jared Stringer

Role	- Company Secretary
Qualifications	- B.Comm (Accounting, Finance), BIT, CPA
Experience	- Began employment with Probiotec in 2002 and accepted role of Financial Accountant in May 2005 before being appointed as Chief Financial Officer in 2011.
Special Responsibilities	- None
Other Directorships	- Nil

Wesley Stringer

Role	- Chief Operation Officer
Qualifications	- B.Comm (Accounting, Finance), LLB (hons), CPA
Experience	- Prior to joining Probiotec, Wesley was employed by KPMG in Taxation and Finance. He has also worked internationally for Deutsche Bank and BNP Paribas Investment Bank in London.
Special Responsibilities	- None
Other Directorships	- Nil

Insurance of Officers

During the financial year the company insured its directors and officers against liabilities for all costs and expenses incurred by them in defending any legal proceedings arising out of their conduct while acting in the capacity as directors and officers of the company, other than conduct involving a willful breach of duty in relation to the company. The total premium paid was $46,242.

REMUNERATION REPORT (AUDITED)

This report is prepared in accordance with section 300A of the Corporations Act 2001 for the Group for the financial year ended 30 June 2012. This report is audited.

1. REMUNERATION

1.1 Remuneration & Nominations Committee

The primary function of the Board Remuneration and Nominations Committee ("Committee") is to assist the Board of Directors ("Board") in fulfilling its oversight responsibility to shareholders by ensuring that:

- the Board comprises individuals best able to discharge the responsibilities of directors having regard to the law and the highest standards of governance; and
- the Group has coherent remuneration policies and practices that fairly and responsibly reward executives having regard to performance, the law and the highest standards of governance.

The Committee's purpose in relation to remuneration is to:

- review and approve executive remuneration policy;
- make recommendations to the Board in relation to the remuneration of the Chief Executive Officer and Non-executive Directors;
- review and make recommendations to the Board on corporate goals and objectives relevant to the remuneration of the Chief Executive Officer, and the performance of the Chief Executive Officer in light of these objectives;
- approve remuneration packages for Probiotec's executives;
- review and approve all equity based plans;
- approve all merit recognition expenditure; and
- oversee general remuneration practices.

The Committee will primarily fulfill these responsibilities by carrying out the activities outlined in its Charter.

The Committee membership and the Chairman of the Committee will be as determined from time to time by the Board. Each of the members will be independent directors and free from any business or other relationship that, in the opinion of the Board, would materially interfere with the exercise of their independent judgement as a member of the Committee. New Committee members will receive induction training from the Chairman of the Committee, the Chief Financial Officer's and GM – Quality's teams and the Company Secretary. Committee members receive continuous training.

Members of Remuneration and Nominations Committee	Position	Appointed	Resigned
Robert Maxwell Johnston	Chairman	29 July 2010	
Maurice Van Ryn	Chairman	28 July 2006	29 July 2010
Graham Buckeridge	Member	28 July 2006	

1.2 Remuneration Policy – Non-Executive Directors

The level of remuneration for the company's non-executive directors is set to reflect the scope of the director's responsibilities, the size of the company's operations and the workload demanded. Probiotec believes that the current remuneration packages for non-executive directors are appropriate having considered the factors above.

The current annualised total remuneration for the company's non-executive directors is $226,000. The Nomination & Remuneration Committee reviews non-executive remuneration annually and makes recommendations to the Board. The Committee considers current market rates of remuneration for similar sized companies and obtains advice from independent professional firms if required. Shareholders will be periodically asked to approve increases in the fee level of non-executive directors if the size, scope, complexity or demands made on the directors increases.

Non-executive directors do not receive any performance related remuneration and are not entitled to receive performance shares, rights or options.

Remuneration levels for non-executive directors for the 2012 financial year are set out on page 24 of this report.

REMUNERATION REPORT (AUDITED) (continued)

1.3 Remuneration Policy – Executive Directors and Key Management Personnel

The Remuneration and Nominations Committee has structured the Group's executive remuneration policies to ensure:

- the policy motivates executives to pursue the long term growth and success of Probiotec within an appropriate control framework;
- the policy demonstrates a clear relationship between individual performance and remuneration; and
- the policy involves an appropriate balance between fixed and variable remuneration, reflecting the short and long term performance objectives appropriate to Probiotec's circumstances and goals.

The Group's remuneration framework for executive directors and key management personnel comprises fixed annual remuneration, short-term incentives and long-term incentives. The Group structures remuneration packages to balance between base incomes and "at risk" incomes to ensure that key personnel are retained, whilst still providing strong incentives to maximise the potential long-term growth of the Group.

Short-term Incentives

Executive directors and key management are eligible to receive short-term incentive payments, in the form of cash bonuses, based on the achievement of set Key Performance Indicators (KPIs). KPIs are based on financial measures targeted at maximising Group performance and returns to shareholders.

Long-term Incentives

The Group provides long-term incentives to key management personnel to reward sustained performance by the organisation as a whole. Long-term incentives are in the form of options over Probiotec Limited shares issued under the company's Exempt Share and Option Plan, which was adopted by a resolution of members on 23 November 2011, or by the issue of shares under the company's Employee Share Plan, which was also adopted by members on 23 November 2011. The issue of shares and/or options is based on a review of the contributions and value of management personnel undertaken by the Nomination and Remuneration Committee.

At the date of this report, Wayne Stringer and Wesley Stringer are the only executive directors of Probiotec Limited. Both are paid a fixed annual remuneration. Along with his fixed annual remuneration, Mr. Wayne Stringer is also eligible to receive equity-based compensation, in the form of share options, based on the achievement of set milestones stipulated in his contract of employment. Mr. Wesley Stringer had previously received shares under the Probiotec Limited Employee Share Plan prior to being appointed as a director of the company.

Termination Arrangements

All key management personnel are employed subject to employment contracts. These employment contracts specify notice period of between one and three months (unless a greater period is required by law). The Group may choose to make a payment in lieu of the notice period.

1.4 Remuneration Policy - Employees

All salaried positions are evaluated based on the size of the role, the level of accountability and experience required, amongst other factors. Economic and market factors are also taken into consideration when evaluating the remuneration level for a specified role.

2. LINKING REMUNERATION TO PROBIOTEC'S PERFORMANCE

Probiotec has structured its remuneration policies to increase goal congruence between shareholders, directors and executives. The company believes that this will have a positive effect on shareholder wealth.

The company is committed to innovation and growth, whilst continuing to focus on maximising profitability and long-term shareholder value.

There is no formal policy linking remuneration policy and company performance.

3. REVIEW OF REMUNERATION

The Remuneration and Nominations Committee meets one to two times per year in conjunction with the release of the financial results or more frequently as circumstances dictate to review the total remuneration paid to the CEO and senior executives of the company. In addition to the members of the Committee, such Executives and/or external parties as the Chairman and members of that Committee think fit may be invited to attend meetings.

All Directors may attend Committee meetings; however, the Chief Executive Officer will have no voting rights and must not be present during discussions on his own remuneration.

4. REMUNERATION DETAILS OF DIRECTORS & KEY MANAGEMENT PERSONNEL

For the purposes of this report, "Key Management Personnel" are defined as those persons that have authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity.

Directors

The following persons were directors of Probiotec Limited during the financial year:

Maurice Van Ryn	Non-executive chairman
Richard David Kuo	Non-executive director
Graham Harry Buckeridge	Non-executive director
Robert Maxwell Johnston	Non-executive director
Charles Wayne Stringer	Executive director
Wesley Stringer	Executive director

Other key management personnel

The following persons also had responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, during the financial year:

Name	Position	Employer
Jared Stringer	Chief Financial Officer	Probiotec Limited
Mark Chatfield	GM – New Business	Probiotec Limited
Dustin Stringer	GM - Marketing	Probiotec Limited
Humera Ahmad	GM - Quality	Probiotec Pharma Pty Ltd
Scott Patterson	GM – Sales	Biotech Pharmaceuticals Pty Ltd

No persons, who were not considered Key Management Personnel during the financial year ended 30 June 2011, were considered Key Management Personnel during this financial year, other than:

Name	Position	Employer
Scott Patterson	GM – Sales	Biotech Pharmaceuticals Pty Ltd

The following persons who were considered Key Management Personnel during the financial year ended 30 June 2011, were no longer considered Key Management Personnel during this financial year:

Name	Position	Employer
Matthew Dalton	GM – Sales	Biotech Pharmaceuticals Pty Ltd
Alan Hong	Group Accountant	Probiotec Limited
David Erasmus	Group Engineering Manager	Biotech Pharmaceuticals Pty Ltd

REMUNERATION REPORT (AUDITED) (continued)

The Directors and identified Key Management Personnel received the following amount of compensation for their services as Directors and executives of the company and the group during the year:

		Short-Term Benefits			Post Employment Benefits		Equity Based Benefits		
2012	**Position**	**Salary, Fees & Commissions $**	**Short Term Incentives $**	**Non-Cash Benefits $**	**Long Service Leave $**	**Superannuation Contribution $**	**Options $**	**Total $**	**Proportion of Remuneration that is performance based (options) %**
Directors & Secretaries									
Maurice Van Ryn	*Chairman*	68,807	-	-	-	6,193	-	75,000	-
Charles Wayne Stringer	*CEO / Managing Director*	665,137	-	-	21,895	59,863	-	746,895	-
Wesley Stringer	*COO / Executive Director*	275,987	-	14,334	3,104	15,679	-	309,104	-
Richard David Kuo	*Non-Executive Director*	55,000	-	-	-	-	-	55,000	-
Graham Harry Buckeridge	*Non-Executive Director*	-	-	-	-	48,000	-	48,000	-
Robert Maxwell Johnston	*Non-Executive Director*	44,036	-	-	-	3,964	-	48,000	-
Jared Stringer	*CFO / Company Secretary*	186,544	-	-	2,543	16,789	-	205,876	-
		1,295,511	**-**	**14,334**	**27,542**	**150,487**	**-**	**1,487,875**	**-**
Other Key Management Personnel									
Dustin Stringer	*GM - Marketing*	169,654	-	-	1,799	15,252	-	184,705	-
Humera Ahmad	*GM - Quality*	153,550	-	-	4,930	22,638	-	181,118	-
Mark Chatfield	*GM – New Business*	151,671	-	-	1,910	26,660	-	180,241	-
Scott Patterson[2]	*GM - Sales*	16,798	-	-	-	10,014	-	26,812	-
		491,673	**-**	**-**	**8,639**	**74,564**	**-**	**574,876**	**-**

[1] *All Long Service Leave amounts relate to accrued balances. No Long Service Leave was taken or paid out during the year*

[2] *Scott Patterson commenced employment on 14 May 2012*

		Short-Term Benefits			Post Employment Benefits		Equity Based Benefits		
2011	**Position**	**Salary, Fees & Commissions $**	**Short Term Incentives $**	**Non-Cash Benefits $**	**Long Service Leave $**	**Superannuation Contribution $**	**Options $**	**Total $**	**Proportion of Remuneration that is performance based (options) %**
Directors & Secretaries									
Maurice Van Ryn	*Chairman*	68,807	-	-	-	6,193	-	75,000	-
Charles Wayne Stringer	*CEO / Managing Director*	617,273	-	-	10,688	55,555	9,415	692,931	1.4
Wesley Stringer	*COO/Executive Director*	263,238	-	27,952	2,278	22,500	5,556	321,524	1.7
Richard David Kuo	*Non-Executive Director*	55,000	-	-	-	-	-	55,000	-
Graham Harry Buckeridge	*Non-Executive Director*	-	-	-	-	48,000	-	48,000	-
Robert Maxwell Johnston	*Non-Executive Director*	51,376	-	-	-	4,624	-	56,000	-
Jared Stringer	*Company Secretary*	155,963	-	-	1,381	14,037	4,167	175,548	2.4
		1,211,657	**-**	**27,952**	**14,347**	**150,909**	**19,138**	**1,424,003**	
Other Key Management Personnel									
Alan Hong	*CFO*	127,209	-	-	1,191	24,683	1,389	154,472	0.9
David Erasmus	*Group Engineering Manager*	121,831	-	4,149	895	13,381	2,315	142,571	1.6
Dustin Stringer[3]	*GM - Europe*	178,381	-	-	1,462	3,716	5,556	189,115	2.9
Humera Ahmad	*GM Quality*	139,947	-	-	3,912	21,606	1,389	166,854	0.8
Mark Chatfield	*GM - Sales & Marketing*	109,809	-	10,340	1,098	16,714	2,315	140,276	1.7
Matthew Dalton	*National Sales Manager*	161,550	-	-	1,723	14,450	5,556	183,279	3.0
		838,727	**-**	**14,489**	**10,281**	**94,550**	**18,520**	**976,567**	

[3] During the year, Dustin Stringer was employed predominantly in the United Kingdom and paid in British pounds. Amounts in this report have been converted into AUD at the average exchange rate for the period of employment.

No long-term employee benefits, other than equity-based benefits have been provided to Directors, Secretaries or Key Management personnel during the year.

REMUNERATION REPORT (AUDITED) (continued)

Options issued to Chief Executive Officer (CEO)

The CEO was appointed in the year 1997. As part of the CEO's remuneration package, options were granted upon the achievement of certain performance targets as set out below. These options are either governed by the Probiotec Limited Exempt Share and Option Plan and vest at the completion of three years of employment from the grant date or are on terms and conditions approved by members in a general meeting. If the CEO resigns prior to the vesting date of the options then the options will be forfeited.

On 5 November 2008, the issue of 1,500,000 options to the CEO was approved at a general meeting on the terms set forth below -

The 1,500,000 options vest as follows:

(a) 500,000 options with an exercise price of $1.50 per share, if the Company's earnings per share (EPS) increases by at least 10% during the financial year ending 30 June 2010 **(2010 Options)**;

(b) 500,000 options with an exercise price of $1.75 per share, if the Company's EPS increases by at least 10% during the financial year ending 30 June 2011 **(2011 Options)**;

(c) 500,000 options with an exercise price of $2.00 per share, if the Company's EPS increases by at least 10% during the financial year ending 30 June 2012 **(2012 Options)**;

(d) Options not vesting as 2010 Options, 2011 Options or 2012 Options do not lapse, but may still vest in 2012 with an exercise price of $2.00 per share if in the 3 year period from 1 July 2009 to 30 June 2012, the Company's EPS has increased by at least 30% **(First Shortfall Options)**,

(e) Options not vesting as 2010 Option, 2011 Options, 2012 Options or First Shortfall Options do not lapse, but may still vest in 2012 with an exercise price of $2.00 per share if in the 4 year period from 1 July 2008 to 30 June 2012, the Company's EPS has increased by at least 65% **(Second Shortfall Options)**,

Regardless of when they vest, the options must be exercised by no later than 30 June 2013.

CEO Employment options

Name	Grant date	Vesting date	Exercise price ($)	Balance at start of the year number	Options granted during the year number	Fair value per option at grant Date ($)
Charles Wayne Stringer	05.11.2008	30.06.2010	1.50	500,000	-	0.21
	05.11.2008	30.06.2011	1.75	500,000	-	0.17
	05.11.2008	30.06.2012	2.00	500,000	-	0.16
				1,500,000	-	

No options were exercised and 700,000 options were forfeited during the year ended 30 June 2012.

5. INTEREST IN SHARES & OPTIONS

The number of shares and options held by directors and key management personnel is as follows:

Name	No. of fully paid ordinary shares	Grant Date	Vesting Date	Expiry Date	Exercise Price	Balance at start of the year number	Option Granted during the year number	Option Vested during the year number	Balance vested at end of the year number	Balance unvested at end of the year number	Fair Value per options[1] at grated date
Maurice Van Ryn	806,101	-	-	-	-	-	-	-	-	-	
Richard David Kuo	74,726	-	-	-	-	-	-	-	-	-	-
Graham Henry Buckeridge	1,348,684	-	-	-	-	-	-	-	-	-	-
Robert Maxwell Johnston	234,000	-	-	-	-	-	-	-	-	-	-
Charles Wayne Stringer	8,357,852	01.7.2009	30.6.2012	30.6.2012	$1.00	400,000	-	-	-	-	$0.06
		01.7.2009	30.6.2012	30.6.2012	$1.00	300,000	-	-	-	-	$0.09
		05.11.2008	30.6.2010	30.6.2013	$1.50	500,000	-	-	-	500,000	$0.21
		05.11.2008	30.6.2011	30.6.2013	$1.75	500,000	-	-	-	500,000	$0.17
		05.11.2008	30.6.2012	30.6.2013	$2.00	500,000	-	-	-	500,000	$0.16
Wesley Stringer	560,745	01.7.2007	30.6.2010	30.6.2012	$1.50	25,000	-	-	-	-	$0.15
		01.7.2008	30.6.2011	30.6.2013	$1.50	50,000	-	-	50,000	-	$0.17
		30.6.2009	30.6.2012	30.6.2014	$2.35	60,000	-	60,000	60,000	-	$0.41
Dustin Stringer	77,000	01.7.2007	30.6.2010	30.6.2012	$1.50	20,000	-	-	-	-	$0.15
		01.7.2008	30.6.2011	30.6.2013	$1.50	40,000	-	-	40,000	-	$0.17
		30.6.2009	30.6.2012	30.6.2014	$2.35	60,000	-	60,000	60,000	-	$0.41
Mark Chatfield	-	01.7.2007	30.6.2010	30.6.2012	$1.50	25,000	-	-	-	-	$0.15
		01.7.2008	30.6.2011	30.6.2013	$1.50	25,000	-	-	25,000	-	$0.17
		30.6.2009	30.6.2012	30.6.2014	$2.35	25,000	-	25,000	25,000	-	$0.41
Humera Ahmad	-	01.7.2007	30.6.2010	30.6.2012	$1.50	25,000	-	-	-	-	$0.15
		01.7.2008	30.6.2011	30.6.2013	$1.50	20,000	-	-	20,000	-	$0.17
		30.6.2009	30.6.2012	30.6.2014	$2.35	15,000	-	15,000	15,000	-	$0.41
Scott Patterson	-	-	-	-	-	-	-	-	-	-	-
Jared Stringer	138,717	01.7.2007	30.6.2010	30.6.2012	$1.50	20,000	-	-	-	-	$0.15
		01.7.2008	30.6.2011	30.6.2013	$1.50	30,000	-	-	30,000	-	$0.17
		30.6.2009	30.6.2012	30.6.2014	$2.35	45,000	-	45,000	45,000	-	$0.41
						2,685,000	-	205,000	370,000	1,500,000	

**The executives have no access to the shares until expiry of 36 months of their employment with the company or an Associated Body Corporate from the date of grant of the shares. All shares are forfeited if the grantee resigns from the company prior to the expiry of 36 months from the date of grant of the shares.*

***All options have been valued using the Black-Scholes option model. The values of the options calculated under this method are allocated evenly over the vesting period.*

REMUNERATION REPORT (AUDITED) (continued)

6. SHARE OPTIONS EXERCISED OR LAPSED DURING THE YEAR

No share options issued to directors or Key Management Personnel were exercised, lapsed or forfeited during the year ended 30 June 2012, other than:

Name	Grant date	Vesting date	Exercise Price ($)	Forfeited during the year Number	Lapsed during the year Number	Value of Shares at Forfeited lapsed Date ($)
Humera Ahmad	01.7.2009	30.6.2010	1.50	-	25,000	0.150*
Mark Chatfield	01.7.2009	30.6.2010	1.50	-	25,000	0.150*
Dustin Stringer	01.7.2009	30.6.2010	1.50	-	20,000	0.150*
Charles Wayne Stringer	01.7.2009	30.6.2012	1.00	-	400,000	0.06*
Charles Wayne Stringer	01.7.2009	30.6.2012	1.00	-	300,000	0.09*
Jared Stringer	01.7.2009	30.6.2010	1.50	-	20,000	0.150*
Wesley Stringer	01.7.2009	30.6.2010	1.50	-	25,000	0.150*

** The fair value of these options at the date lapsed was $0.01 per option.*

The board has no formal policy in place for limiting the risk to the directors or other key management personnel in relation to the options issued.

7. CONTRACTS OF EMPLOYMENT

All executive staff employed by the Group are subject to employment contracts, which set out the terms and conditions of their employment. These contracts define their level of remuneration, length of contract (if for fixed period) and termination events amongst other areas. The standard notice period for employees of the Group is one month; however, this may be varied to be up to one year in limited instances.

End of remuneration report.

Proceedings on Behalf of the Company

No person has applied for leave of court to bring proceedings on behalf of the company or intervene in any proceedings to which the company is a party for the purpose of taking responsibility on behalf of the company for all or any part of those proceedings.

Non-audit Services

The board of directors is satisfied that the provision of non-audit services during the year is compatible with the general standard of independence for auditors imposed by the Corporations Act 2001. The directors are satisfied that the services disclosed below did not compromise the external auditor's independence for the following reasons:

- all non-audited services are reviewed and approved by the board prior to commencement to ensure that they do not adversely affect the integrity and objectivity of the auditor; and
- the nature of the services provided do not compromise the general principles relating to auditors independence as set out in Code of Conduct APES 110 Code of Ethics for professional accountants issued by the Accounting professional & ethical standards board, including reviewing or auditing the auditor's own work, acting in a management or decision making capacity for the company, acting as advocate for the company or jointly sharing economic risks and rewards.

No fees for non-audit services were paid/payable to the external auditors during the year ended 30 June 2012.

Auditor's Independence Declaration

A copy of the auditor's independence declaration as required under section 307C of the Corporations Act 2001 is set out on page 29 of this report.

Signed in accordance with a resolution of Board of Directors.

Director
Charles Wayne Stringer

Signed at Laverton this 28th day of August 2012

AUDITOR'S INDEPENDENCE DECLARATION

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ACCOUNTANTS & ADVISORS

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Auditor's Independence Declaration under Section 307C of the Corporations Act 2001 to the directors of Probiotec Limited

I declare that, to the best of my knowledge and belief, during the year ended 30 June 2012 there have been:

(i) No contraventions of the auditor independence requirements as set out in the Corporations Act 2001 in relation to the audit, and

(ii) No contraventions of any applicable code of professional conduct in relation to the audit.

Moore Stephens

MOORE STEPHENS
Chartered Accountants

Nick Michael
Partner

Melbourne, 28 August 2012

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 30 JUNE 2012

	Note	Consolidated Group 2012 $	2011 $
Sales revenue from continuing operations	2	66,046,188	71,770,144
Cost of goods sold		(36,791,522)	(37,840,561)
Gross profit		29,254,666	33,929,583
Other revenue	2	119,164	111,716
Other income	2	3,585,907	493,338
Warehousing & distribution expenses		(4,778,448)	(5,286,986)
Sales and marketing expenses		(14,138,251)	(15,426,901)
Impairment expenses		(1,245)	(3,115,527)
Finance costs		(2,011,984)	(2,277,535)
Legal costs		(418,818)	(215,923)
Administration and other expenses	4	(9,373,374)	(9,948,790)
Profit / (loss) from continuing activities before income tax expense		**2,237,617**	**(1,737,025)**
Income tax expense relating to continuing activities	5	(8,367)	(345,624)
Profit / (loss) from continuing activities for the period attributable to members of the parent entity		**2,229,250**	**(2,082,649)**
Loss from discontinued operations	6	(979,870)	(8,255,138)
Profit for the period attributable to members of the parent entity	3	**1,249,380**	**(10,337,786)**
Other comprehensive income			
Other Comprehensive income		(90,584)	(965,379)
Income tax on items of other comprehensive income		-	-
Other comprehensive income for the year, net of tax		(90,584)	(965,379)
Total comprehensive income for the year		1,158,796	(11,303,166)
Total comprehensive income for the year attributable to members of the parent entity		1,158,796	(11,303,166)
Earnings per share for profit attributable to members of the parent entity			
Basic earnings per share (cents)	31	2.4	(19.5)
Diluted earnings per share (cents)	31	2.4	(19.5)
Earnings per share from discontinued operations			
Basic earnings per share (cents)	31	(1.9)	(15.6)
Diluted earnings per share (cents)	31	(1.9)	(15.6)

The Consolidated Statement of Comprehensive Income is to be read in conjunction with the attached notes.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT 30 JUNE 2012

	Note	Consolidated Group 2012 $	2011 $
Current Assets			
Cash and cash equivalents	11	193,388	938,107
Trade and other receivables	12	8,446,915	10,250,305
Inventories	13	14,253,617	14,813,261
Other current assets	14	489,770	415,305
Total Current Assets		**23,383,690**	**26,416,978**
Non-Current Assets			
Loans receivable	16	-	596,817
Property, plant and equipment	17	47,938,462	48,583,593
Intangible assets	18	28,332,961	29,558,853
Deferred tax assets	19	1,510,279	1,405,515
Total Non-Current Assets		**77,781,702**	**80,144,778**
Total Assets		**101,165,392**	**106,561,756**
Current Liabilities			
Trade & other payables	20	10,213,722	11,471,790
Short-term interest bearing liabilities	21	21,779,416	27,178,140
Current tax liabilities	5	-	3,071
Short-term provisions	22	969,210	894,791
Total Current Liabilities		**32,962,348**	**39,547,792**
Non-Current Liabilities			
Long-term interest bearing liabilities	21	2,049,986	2,126,086
Deferred tax liabilities	23	3,330,902	3,291,532
Long-term provisions	22	348,006	280,993
Total Non-Current Liabilities		**5,728,894**	**5,698,611**
Total Liabilities		**38,691,242**	**45,246,403**
Net Assets		**62,474,150**	**61,315,353**
Equity			
Contributed equity	24	35,072,269	36,581,517
Shares held by equity compensation plan	25	(1,385,750)	(2,894,998)
Reserves	26	3,558,724	3,842,079
Retained earnings		25,228,907	23,786,755
Total Equity		**62,474,150**	**61,315,353**

The Consolidated Statement of Financial Position is to be read in conjunction with the attached notes.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 30 JUNE 2012

	Note	Ordinary Share Capital $	Shares held by Equity Compensation Plan $	Reserves $	Retained Earnings $	Total $
Balance as at 1 July 2010		36,360,891	(2,894,998)	4,807,458	35,180,125	73,453,476
Total comprehensive income for the year						
Profit for the year		-	-	-	(10,337,787)	(10,337,787)
Other comprehensive income		-	-	(965,379)	-	(965,379)
Total comprehensive income for the year		**-**	**-**	**(965,379)**	**(10,337,787)**	**(11,303,166)**
Transactions with owners in their capacity as owners						
Shares issued during the year		220,626	-	-	-	220,626
Dividends paid or provided for		-	-	-	(1,055,583)	(1,055,583)
Balance as at 30 June 2011		**36,581,517**	**(2,894,998)**	**3,842,079**	**23,786,755**	**61,315,353**
Total comprehensive income for the year						
Profit for the year		-	-	-	1,249,380	1,249,380
Asset revaluations		-	-	(306,236)	-	(306,236)
Other comprehensive income		-	-	22,881	192,771	215,652
Total comprehensive income for the year		**-**	**-**	**(283,355)**	**1,442,151**	**1,158,796**
Transactions with owners in their capacity as owners						
Shares (cancelled) issued during the year		(1,509,248)	1,509,248	-	-	-
Dividends paid or provided for		-	-	-	-	-
Balance as at 30 June 2012		**35,072,269**	**(1,385,750)**	**3,558,724**	**25,228,907**	**62,474,150**

The Consolidated Statement of Changes in Equity is to be read in conjunction with the attached notes.

CONSOLIDATED STATEMENT OF CASH FLOWS
AS AT 30 JUNE 2012

	Note	Consolidated Group 2012 $	2011 $
Cash Flows From Operating Activities			
Receipts from customers		67,849,578	75,510,809
Payments to suppliers and employees		(62,410,161)	(66,796,732)
Interest received		119,164	111,716
Interest and other costs of finance paid		(2,011,984)	(2,277,535)
Income tax paid		(3,071)	(229,192)
Net cash provided by operating activities	30 (b)	3,543,527	6,319,066
Cash Flows From Investing Activities			
Payment for property, plant and equipment		(3,532,926)	(2,012,157)
Proceeds from sale of property, plant and equipment		1,048,125	-
Proceeds from sale of intangible assets		6,000,000	-
Cash payments for investments, net of cash acquired		(322,046)	-
Receipts relating to loans receivable		590,001	519,499
Purchase of intangible assets		(2,596,575)	(1,933,653)
Net cash used in investing activities		1,186,579	(3,426,311)
Cash Flows From Financing Activities			
Proceeds from issues of shares		-	220,626
Dividends Paid		-	(1,055,583)
Proceeds from borrowings		1,527,448	277,124
Repayment of borrowings		(7,002,271)	(4,213,230)
Net cash provided by / (used in) financing activities		(5,474,823)	(4,771,063)
Net Increase in cash held		(744,719)	(1,878,308)
Cash at beginning of financial year		**938,107**	**2,816,415**
Cash at end of financial year	11	**193,388**	**938,107**

The Consolidated Statement of Cash Flows is to be read in conjunction with the attached notes.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2012

1. STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES

The financial report covers Probiotec Limited ("company") and controlled entities ("group"). Probiotec Limited is a for-profit listed public company, incorporated and domiciled in Australia. The financial report is for the financial year ended 30 June 2012 and is presented in Australian dollars.

Basis of Preparation

The financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards, Australian Accounting interpretations, other authoritative pronouncements of the Australian Accounting Standards Board (AASB) and the Corporations Act 2001.

The accounting policies set out below have been consistently applied to all years presented.

Reporting Basis and Convention

The financial report has been prepared on an accrual basis and is applied on historical costs modified by the revaluation of selected non-current assets, financial liabilities and derivative financial instruments for which the fair value basis of accounting has been applied.

Compliance with IFRS

Australian Accounting Standards include International Financial Reporting Standards as adopted in Australia. Compliance with Australian Accounting Standards ensures that the financial statements and notes of Probiotec Limited comply with International Financial Reporting Standards (IFRS). Material accounting policies adopted in the preparation of these financial statements have been consistently applied unless stated otherwise.

Accounting Policies

(a) Principles of Consolidation

The consolidated financial statements are prepared by combining the financial statements of all the entities that comprise the consolidated entity, being Probiotec Limited (the parent entity) and its controlled entities as defined in accounting standard AASB 127 "Consolidated and Separate Financial Statements". Where a subsidiary either began or ceased to be controlled during the year, the results of its operations are included only from the date control commenced or ceased.

All inter-company balances and transactions between entities in the group, including any unrealised profits or losses, have been eliminated on consolidation.

Minority interests in the results and equity of subsidiaries are shown separately in the consolidated statement of comprehensive income and statement of financial position respectively.

Subsidiaries are accounted for by the parent entity at cost, less any impairment charges.

(b) Income Tax

(i) General

Current tax assets and liabilities for the current and prior periods are measured as the amount expected to be recovered from or paid to the taxation authorities. The income tax expense for the period is the tax payable on the current period's taxable income based on the notional income tax rate of each jurisdiction adjusted by changes in deferred tax assets and liabilities attributable to temporary differences between the tax base of assets and liabilities and their carrying amounts in the financial statements, and to unused tax losses.

Deferred tax balances are determined using the balance sheet liability method which calculates temporary differences based on the carrying amounts of an entity's asset and liabilities carried in the financial statements and their associated tax bases. No deferred income tax will be recognised from the initial recognition of an asset or liability, excluding a business combination, where there is no effect on accounting or taxable profit or loss.

The amount of deferred tax provided will be based on the expected manner of realisation of the asset or settlement of the liability, using tax rates enacted on reporting date. Deferred tax is credited in profit or loss except where it relates to items that may be credited directly to equity, in which case the deferred tax is adjusted directly against equity.

Deferred tax assets will be recognised only to the extent that it is probable that future income tax profits will be available against which the assets can be utilised. The amount of benefits brought to account or which may be realised in the future is based on the assumption that no adverse change will occur in income taxation legislation and the anticipation that the group will derive sufficient future assessable income to enable the benefit to be realised and to comply with the conditions of the deductibility imposed by law.

The carrying amount of deferred income tax assets is reviewed at each balance date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax to be utilised.

Unrecognised deferred income tax assets are reassessed at each balance date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

(ii) Goods and Services Tax

Revenues, expenses and assets are recognised net of the amount of GST, except where the amount of GST incurred is not recoverable from the Australian Taxation Office. In these circumstances the GST is recognised as part the cost of acquisition of the asset or as part of an item of the expense. Receivables and payables in the statement of financial position are shown inclusive of GST.

Cash flows are included in the statement of cash flows on a gross basis and the GST component of cash flows arising from investing and financing activities, which is recoverable from, or payable to, the taxation authority are classified as operating cash flows. Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

(c) Foreign Currency Translation

(i) Functional and presentation currency

The functional currency of each of the group's entities is measured using the currency of the primary economic environment in which that entity operates. The consolidated financial statements are presented in Australian dollars which is the parent entity's functional and presentation currency.

(ii) Foreign Currency Transactions

Foreign currency transactions are translated into the functional currency using the exchange rate prevailing at the date of the transaction. Foreign currency monetary items are translated at the year end exchange rate. Non-monetary items measured at historical cost continue to be carried at the exchange rate at the date of the transaction. Non-monetary items measured at fair value in a foreign currency are translated at the date when the fair value was determined.

(iii) Translation of group companies functional currency to presentation currency

The results of the New Zealand, British, Chinese, German and Irish subsidiaries are translated into Australian dollars as at the date of the transactions. Assets and liabilities are translated at exchange rates prevailing at balance date.

Exchange variations resulting from the translation are recognised in the foreign currency translation reserve in other comprehensive income.

(d) Impairment of assets

The recoverable amount of the Group assets excluding deferred tax assets and goodwill are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the asset is tested for impairment by comparing the recoverable amount (being the higher of the asset's fair value less cost to sell and value in use) to its carrying amount. Goodwill and intangible assets that have an indefinite useful life and assets not ready for use are tested for impairment at least annually. The recoverable amount is estimated for the individual asset or, if it is not possible to estimate the recoverable amount for the individual asset, the recoverable amount of the cash generating unit (CGU) to which the asset belongs is determined. CGUs have been determined as the smallest identifiable group of assets that generate cash inflows largely independent of the cash flow of other assets.

An impairment loss is recognised as an expense when the carrying amount of an asset or the CGU exceeds its recoverable amount. Impairment losses recognised in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the CGU and then, to reduce the carrying amount of the other assets in the unit on a pro rata basis.

An impairment loss recognised in prior periods for an asset (other than goodwill) is reversed if, and only where there is an indicator that the impairment loss may no longer exist, and there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. The increased carrying amount of an asset due to a reversal of an impairment loss does not exceed the carrying amount that would have been determined (net of amortisation) had no impairment loss been recognised for the asset in prior years.

In calculating the value in use, the cash flow includes projections of cash inflows and outflows from continuing use of the asset and cash flows associated with disposal of the asset. The cash flows are estimated for the assets in their current condition and do not include cash flows and out flows expected to arise from future restructuring which are not yet committed, or from improving or enhancing the asset's performance.
In assessing value in use, the estimated cash flows are discounted to their present value effectively using a pre-tax discount rate that reflects the current market assessments of the risk specific to the asset or CGU.

(e) Inventories

Inventories, which include raw materials, work in progress and finished goods, are valued at the lower of cost and net realisable value. Costs comprise all cost of purchase and conversion, including material, labour and appropriate portion of fixed and variable overhead expenses. Costs have been assigned to inventory on hand at reporting date using either the first-in-first-out (F.I.F.O.) basis or the weighted average cost basis, depending on the nature of product being manufactured. Fixed overheads are allocated on the basis of normal operating capacity. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated cost of completion and selling expenses.

(f) Property, Plant and Equipment

Each class of property, plant and equipment is carried at historical cost or fair value less accumulated depreciation and impairment. Cost includes expenditure that is directly attributable to the acquisition of the item.

(i) Property

Freehold land and buildings are stated at fair value (being the amount for which an asset could be exchanged between knowledgeable willing parties in an arm's length transaction), based on periodic, valuations by external valuers, less subsequent depreciation for the building. Any accumulated depreciation at the date of valuation is eliminated against the gross carrying amount of the asset and the net amount is reinstated to the revalued amount of the asset. Independent valuations are carried out every three to five years, with internal reviews performed regularly to ensure that the carrying amounts of land and buildings do not differ materially from the fair value at the reporting date.

Increases in the carrying amount arising on revaluation of land and buildings are credited to a revaluation reserve in equity. Decreases that offset previous increases of the same asset are charged against fair value reserves directly in equity; all other decreases are charged to profit or loss. Each year the difference between depreciation based on the revalued carrying amount of the asset charged to profit or loss and depreciation based on the asset's original cost is transferred from the revaluation reserve to retained earnings. When revalued assets are sold, amounts included in the revaluation reserve relating to the asset are transferred to retained earnings.

(ii) Plant and Equipment

Plant and equipment are stated at historical cost, including costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management, less depreciation and any impairments.

The carrying amount of plant and equipment is reviewed annually by directors to ensure it is not in excess of the recoverable amount from these assets. The recoverable amount is assessed as the higher of fair value less costs to sell or value in use. In the event the carrying amount of plant and equipment is greater than the estimated recoverable amount, the carrying amount is written down immediately to the estimated recoverable amount and impairment losses are recognized either in profit and loss or as a revaluation decrease if the impairment loss relates to a revalued asset.

The cost of fixed assets constructed within the group includes the cost of materials, direct labour, borrowing costs and an appropriate proportion of fixed and variable overheads. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the profit or loss during the financial year in which they were incurred.

Depreciation

The depreciable amount of property, plant and equipment, including capitalised lease assets, but excluding freehold land, is depreciated on a straight line basis over their useful lives to the group commencing from the time the asset is held ready for use. Leasehold improvements are depreciated over the shorter of either the unexpired period of the lease or the estimated useful lives of the improvements.

The depreciation rates used for each class of depreciable assets are:

Buildings	4%
Leased Plant, Equipment and Other	5% to 12.5%
Plant, Equipment and Other	5% to 50%

The assets' residual value and useful life are reviewed, and adjusted if appropriate, at each balance date.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount. These gains and losses are included in profit or loss.

(g) Leases

Leases where substantially all the risks and benefits incidental to the ownership of the asset, but not the legal ownership, are transferred to the entities within the group are classified as finance leases. Finance lease are capitalised at the lower of the fair value of the leased property or the present value of the minimum lease payments. The corresponding rental obligations, net of finance charges, are included in the current and non-current interest bearing liabilities. Each lease payment is allocated between the liability and the finance charges. The interest element of the lease payment is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The property, plant and equipment acquired under finance leases is depreciated over the shorter of the asset's useful life or the lease term, unless it is reasonably certain that ownership will be obtained by the end of the lease term where it is depreciated over the period of the expected use which is the useful life of the asset.

Lease payments for operating leases, where substantially all the risks and benefits remain with the lessor, are charged as expenses on a straight line basis over the period of the lease.

(h) Investments in Associates

Associates comprise entities over which the parent entity or the Group have significant influence and hold an ownership interest. Investments in associated companies are recognised in the financial statements by applying the equity method of accounting.

Under the equity method of accounting the carrying amounts of investments in associates are increased or decreased to recognise the Group's share of the post-acquisition profits or losses and other changes in net assets of the associates. The Group's share of the post-acquisition profits or losses of associates is included in the consolidated profit and loss.

The financial statements of the associate are used to apply the equity method. The reporting dates of the associate and the parent are identical and both use consistent accounting policies.

Associates are accounted for in the parent entity financial statements at cost.

(i) Interests in Joint Venture Entities

Under AASB 131 "Interests in Joint Ventures" interests in jointly controlled entities can be recognised using either the proportionate consolidation approach or the equity method. Prior to 1 July 2008, the group had accounted for its interests in joint ventures using the equity method. From 1 July 2008, the group has changed its policy to account for interests in joint ventures such that the proportionate consolidation method is adopted.

(j) Intangibles

i) Goodwill

Goodwill on consolidation is initially recorded at the amount by which the purchase price for a business or for an ownership interest in a controlled entity exceeds the fair value attributed to the acquiree's identifiable assets, liabilities and contingent liabilities at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in intangible assets. Goodwill on acquisition of associates is included in investments in associates. Goodwill is tested annually for impairment. For the purpose of impairment testing, goodwill acquired in a business combination is allocated to each of the group's cash-generating units, or groups of cash-generating units that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the group are assigned to these units or groups of units. Impairment is determined by assessing the recoverable amount of the cash-generating unit, or group of cash-generating units, to which the goodwill relates. Impairment losses recognised for goodwill are not subsequently reversed. Goodwill is carried at cost less accumulated impairment losses. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

ii) Trademarks, Licenses, product development costs and Product Dossiers

Trademarks, licenses, product development costs and product dossiers ("Developed Products") are initially recognised at cost. Developed Products have an indefinite life and are tested at each reporting date for impairment and carried at cost less accumulated impairment losses. Those with a finite life are carried at cost less any accumulated amortisation and accumulated impairment losses. Those developed products with finite lives are amortised on a straight line basis over a useful life of between 10 and 40 years. Amortisation is included within administration and other expenses in the statement of comprehensive income.

iii) Research and Development – Internally generated

Research costs are expensed as incurred. Development expenditure incurred on an individual project is capitalised if the product or service is technically feasible, adequate resources are available to complete the project, it is probable that future economic benefits will be generated and expenditure attributable to the project can be measured reliably. Expenditure capitalised comprises costs of materials, services, direct labour and directly attributable overheads. Other development costs are expensed when they are incurred. Capitalised development expenditure is stated at cost less accumulated amortisation and any impairment losses and amortised over the period of expected future sales from the related projects. The carrying value of development costs is reviewed annually when the asset is not yet available for use, or when events or circumstances indicate that the carrying value may be impaired.

(k) Employee Benefits

i) Wages, Salaries & Annual Leave

Liabilities for employee benefits such as wages, salaries, annual leave, sick leave and other current employee entitlements represent present obligations resulting from employees' services provided to reporting date, and are measured at the amount expected to be paid when the liabilities are settled.

ii) Long Service Leave

Liabilities relating to Long Service Leave are measured as the present value of the estimated future cash outflows to be made in respect to services provided by employees, up to the reporting date. Consideration is given to expected future wage levels, experience of employee departures and period of service. Expected future payments are discounted using market yields at the reporting date on national government bonds with terms to maturity that match, as closely as possible, the estimated future cash outflows.

iii) Superannuation

Contributions are made by the entity to employee superannuation funds and are charged as expenses when incurred. The consolidated entity does not maintain any retirement benefit funds.

iv) Employee share based payments

Shares issued pursuant to an employee share plan, which are facilitated by means of a loan with recourse only to the shares, are treated as an option grant. The loan is shown as a reduction in equity until the shares are either cancelled or settled in accordance with the terms of the plan. The fair value of options granted is recognised as an employee benefit expense with a corresponding increase in the share-based payments reserve in equity. The fair value is measured at grant date taking into account market performance conditions only, and spread over the vesting period during which the employees become unconditionally entitled to the options. The fair value of options granted is measured using the Black Scholes model. The amount recognised as an expense is adjusted to reflect the actual number of options that vest, except where forfeiture is due to market related conditions.

At each subsequent reporting date until vesting, the cumulative change to profit or loss is the product of:

- The grant date fair value.
- The current best estimate of the number of securities that will vest, taking into account factors such as the likelihood of employee turnover during the vesting period and the likelihood of non-market performance conditions not being met.
- The expired portion of the vesting period.

(l) Financial Instruments

Recognition

Financial instruments are initially measured at fair value plus directly attributable transaction costs. Subsequent to initial recognition these instruments are measured as set out below.

Financial assets at fair value through profit and loss

A financial asset is classified in this category if acquired principally for the purpose of selling in the short term with the intention of making a profit or if so designated by management and within the requirements of AASB 139: Financial Instruments: Recognition and Measurement. Derivatives are also categorised as held for trading unless they are designated as hedges. Realised and unrealised gains and losses arising from derivatives and changes in the fair value of these assets are included in profit or loss in the period they arise.

Loans and Receivables

Loan and Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and are stated at amortised cost using the effective interest method. Loans and receivables are initially measured at fair value and are subsequently measured at amortised cost less any allowance for impairment. Trading terms are between 7 days to 60 days. An allowance for impairment is recognised when it becomes improbable that the all or part of the loan or receivable will be recoverable. Gains or losses are recognised in profit or loss when the loans and receivables are derecognised or impaired.

Held to maturity Investments

These investments have fixed or determinable payments and fixed maturities, and it is the group's intention to hold these investments to maturity. Any held-to-maturity investments held by the group are stated at amortised cost using the effective interest method. Gains or losses are recognized in profit or loss through the amortization process and when the financial asset is derecognized.

Available for sale financial assets

Available for sale financial assets include any non-derivative financial assets that are designated as available for sale or that are not included in the above categories. Available for sale financial assets are reflected at fair value. After initial recognition available-for-sale assets are measured at fair value. Unrealised gains or losses arising from changes in fair value are recognized in other comprehensive income when the financial asset is derecognized, the cumulative gain or loss pertaining to that asset previously recognized in other comprehensive income is reclassified into profit or loss.

Trade and other payables

Trade and other payables represent liabilities for goods and services provided to the group prior to the year end and which are unpaid. These amounts are unsecured and have 30 – 90 day payment terms. Trade and other payables are carried at amortised cost, yet due to their short term nature, they are not discounted. Gains or losses are recognized in profit or loss through the amortization process when the financial liability is derecognized.

Interest bearing liabilities

All loans and borrowings are initially recognised at fair value, net of directly attributable transaction costs incurred. Borrowings are subsequently measured at amortised cost using the effective interest method.

Fair Value

Fair value is determined based on current bid prices of all quoted investments. Valuation techniques are applied to determine the fair value for all unlisted securities, including recent arm's length transactions, reference to similar instruments and option pricing models.

Impairment

At each reporting date, the group assesses whether there is objective evidence that a financial instrument has been impaired.

Derivative financial instruments

The group uses derivative financial instruments such as forward foreign currency contracts and interest rate swaps to hedge its risk associated with interest rate and foreign currency fluctuations. Such derivatives are stated at fair value on the date which the derivative contract is entered into and is subsequently remeasured at fair value. The fair value of forward exchange contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles. The fair value of interest rate swap contracts is determined by reference to market values for similar instruments.

For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to net profit or loss for the year where they are material.

(m) Government Grants

Grants from government are recognised at the fair value when there is a reasonable assurance that the grant will be received and the consolidated entity has complied with the required conditions. Grants relating to expense items are recognised as income over the periods necessary to match the grant to the costs they are compensating. Grants relating to assets are credited to deferred income and are amortised on a straight line basis over the expected lives of the assets.

(n) Revenue Recognition

Revenue is measured at the fair value of the consideration received or receivable to the extent it is probable that the economic benefits will flow to the group and the revenue can be measured reliably. Amounts disclosed as revenue are net of returns, allowances and discounts. Sales revenue comprises revenue earned from the provision of products and services to entities outside the consolidated entity. Sales revenue is recognised when the risks and rewards of ownership have transferred to the customer and can be measured reliably. Risks and rewards are considered passed to the buyer when goods have been delivered to the customer.

Interest income is recognised as it accrues using the effective interest method. This method uses the effective interest rate which is the rate that exactly discounts the estimated future cash receipts over the expected life of the financial asset to the net carrying amount of the financial asset. Interest income is included as financial income in profit or loss. Dividends are recognised when the group's right to receive payment is established.

All revenue is stated net of the amount of goods and services tax (GST).

(o) Financing costs

Financing costs include interest income and expense, amortisation of discounts or premiums relating to borrowings, amortisation of ancillary costs incurred in connection with the arrangement of borrowings and lease finance charges. Borrowing costs are expensed as incurred except when directly attributable to the acquisition, construction or production of a qualifying asset, in which case they form part of the cost of the asset.

(p) Provisions

A provision is recognised when there is a legal or constructive obligation as a result of a past event and it is probable that a future sacrifice of economic benefits will be required to settle the obligation, and the amount can be reliably estimated. Provisions are not recognised for future operating losses. Provisions are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the reporting date using a discounted cash flow methodology.

(q) Cash

For purposes of the statement of cash flows, cash includes deposits at call with financial institutions which are readily convertible to cash on hand and are subject to an insignificant risk of changes in value, net of outstanding bank overdrafts.

(r) Comparative Figures

Comparative figures have been adjusted to conform to changes in presentation for the current year.

(s) Earnings per share

Basic earnings per share is determined by dividing the net profit attributable to members of the Company, excluding any costs of servicing equity other than ordinary shares, by the weighted average number of ordinary shares, adjusted for any bonus elements.

Diluted earnings per share is determined by dividing the net profit attributable to members of the Company, by the weighted average number of ordinary shares and dilutive potential ordinary shares adjusted for any bonus elements.

(t) Contributed equity

Issued and paid up capital is recognised at the fair value of the consideration received by the Company.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

(u) Shares held by equity compensation plan

If shares are issued pursuant to an employee share plan, which are facilitated by means of a loan with recourse only to the shares, they are treated as an option grant. The loan is recognised in the shares held by equity compensation plan account (shown as a reduction in equity) until the shares are either cancelled or settled in accordance with the terms of the plan, upon which the shares held by equity compensation plan account is credited.

(v) Business combinations

The acquisition method of accounting is used to account for all business combinations, including business combinations involving entities or businesses under common control, regardless of whether equity instruments or other assets are acquired. The consideration transferred for the acquisition of a subsidiary comprises the fair values of the assets transferred, the liabilities incurred and the equity interests issued by the group. The consideration transferred also includes the fair value of any contingent consideration arrangement and the fair value of any pre-existing equity interest in the subsidiary. Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are, with limited exceptions, measured initially at their fair values at the acquisition date. On an acquisition-by-acquisition basis, the group recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net identifiable assets.

The excess of the consideration transferred, the amount of any non-controlling interest in the acquire and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the group's share of the net identifiable assets acquired is recorded as goodwill. If those amounts are less than the fair value of the net identifiable assets of the subsidiary acquired and the measurement of all amounts has been reviewed, the difference is recognised directly in profit or loss as a bargain purchase.

Where settlement of any part of cash consideration is deferred, the amounts payable in the future are discounted to their present value as at the date of exchange. The discount rate used is the entity's incremental borrowing rate, being the rate at which a similar borrowing could be obtained from an independent financier under comparable terms and conditions.

(w) Working capital deficiency

As presented in the statement of financial position, the group has a net working capital deficiency of $9,578,658. This is caused by $18,065,968 worth of liabilities which exist under a facility due to expire on dates subsequent to 30 June 2013 being classified as current due to an annual review clause included in the finance facility which would require the group to repay the debt if the bank was not satisfied with the financial condition of the group. The group has complied with all financial covenants within the finance facility and there have been no indications given by the financier that they intend to recall any portion of the debt prior to the expiry date of the finance facility. Excluding these loans, the group has a net working capital balance of $8,487,310 and believes that it will continue as a going concern for a period of 12 months from the date of the director's declaration.

(x) New Accounting Standards

Certain new accounting standards and interpretations have been published that are not mandatory for 30 June 2012 reporting periods, and have not yet been adopted by the Group. The Group's and the parent entity's assessment of the impact of these new standards and interpretations is set out below.

- AASB 9 *Financial Instruments*, AASB 2009-11 *Amendments to Australian Accounting Standards arising from the* AASB 9 sets out requirements for the classification and measurement of financial assets. AASB 2008-6 will become mandatory for the Group's 30 June 2014 financial statements. The Group will apply this revised AASB 2009-11 from 30 June 2014 but it is not expected to have any impact on the Group's financial statements.
- AASB 2010-8 *Amendment to Australian Accounting Standards – Deferred Tax: Recovery of Underlying Assets* provide a practical approach for measuring deferred tax liabilities and deferred tax assets when investment property is measured using the fair value model in AASB 140 *Investment Property*. AASB 2010-8 will become mandatory for the Group's 30 June 2013 financial statements. The Group will apply this revised AASB 2010-8 from 30 June 2013 but it is not expected to have any impact on the Group's financial statements.
- AASB 10: *Consolidated Financial Statement* s provides a revised definition of control and additional application guidance so that a single control model applies to all investees. The Group has not yet been able to reasonably estimate the impact of this Standard on its financial statements.
- AASB 11 *Joint Arrangements* requires joint arrangements to be classified as either "joint operations" (where the parties that have joint control of the arrangement have rights to the assets and obligations for the liabilities) or "joint ventures" (where the parties that have joint control of the arrangement have rights to the net assets of the arrangement). Joint ventures are required to adopt the equity method of accounting (proportionate consolidation is no longer allowed).
- AASB 12 *Disclosure of Interests in Other Entities* contains the disclosure requirements applicable to entities that hold an interest in a subsidiary, joint venture, joint operation or associate. AASB 12 also introduces the concept of a "structured entity", replacing the "special purpose entity" concept currently used in interpretation 112, and requires specific disclosures in respect of any investments in unconsolidated structured entities. This standard will affect disclosures only and is not expected to significantly affect the Group.
- To facilitate the application of AASBs 10, 11 and 12, revised versions of AASB 127 and AASB 128 have also been issued. These Standards are not expected to significantly impact the Group.

NOTES TO THE FINANCIAL STATEMENTS (continued)

	2012 $	2011 $
2. REVENUE AND OTHER INCOME		
Revenue from:		
Interest received	119,164	111,716
Sale of goods	66,046,188	71,770,144
Total Revenue	**66,165,352**	**71,881,860**
Government subsidies received	174,389	224,147
Profit on disposal of intangible assets	2,663,862	-
Sundry income	747,656	269,191
Total other income	3,585,907	493,338
Total revenue and other income from continuing operations	**69,751,259**	**72,375,198**
Sales revenue from discontinued operations	418,321	1,713,260
Interest income from discontinued operations	493	493
Total revenue and other income from discontinued operations	**418,814**	**1,713,753**
3. PROFIT FOR THE YEAR		
Net profit has been arrived at after including:		
Finance cost - non related parties	2,011,984	2,277,535
Foreign currency translation losses	675,545	223,664
Bad and doubtful debts expense	43,919	347,500
Rental on operating lease expenses	612,337	774,996
Inventory write-offs	257,069	2,685,676
Professional and consulting expenses	188,864	278,579
Employee benefits expenses	22,082,681	21,365,518
Repairs and maintenance expenses	795,436	871,443
Research and development cost	2,183,790	3,494,615
Depreciation of property, plant and equipment	3,129,932	3,566,216
Amortisation of intangibles	694,327	324,384
Impairment costs - intangibles	1,245	3,774,476
Impairment costs - current assets	991,182	-
Impairment - investments	385,767	-
Impairment costs - property, plant and equipment	-	2,041,031
Defined contribution superannuation expense	966,442	1,288,457
4. ADMINISTRATION & OTHER EXPENSES		
Administration & other expenses comprises:		
Insurance	862,280	867,850
Office expenses	920,445	931,913
Travel and entertainment	493,780	398,327
Compliance costs	867,571	391,698
Other expenses	6,229,298	7,359,002
	9,373,374	**9,948,790**

	2012 $	2011 $
5. INCOME TAX EXPENSE		
(a) Components of Tax Expense:		
Current income tax	-	83,015
Deferred income tax	8,367	(1,330,386)
Over provision for income tax in prior years	-	(86,401)
	8,367	**(1,333,772)**
Income tax is attributable to:		
(Loss) / profit from continuing operations	8,367	345,624
(Loss) / profit from discontinued operations	-	(1,679,396)
	8,367	**(1,333,772)**
(b) Reconciliation of income tax expense to prima facie tax payable on profit / (loss)		
Profit / (loss) from continuing operations	2,237,617	(1,737,025)
Profit / (loss) from discontinued operations	(979,870)	(9,934,534)
	1,257,747	**(11,671,559)**
Prima facie tax expense on profit/(loss) before income tax at 30% (2011: 30%)	377,324	(3,501,468)
Add Tax effect of:		
Impairment of intangibles	374	934,658
Impairment of fixed assets	-	672,193
Recoupment of prior losses not yet booked	(150,000)	(570,537)
Tax losses not recognised	-	1,679,396
Research and development tax concession	(135,000)	(168,773)
Other non allowable or assessable items	(84,331)	(379,241)
Income tax expense / (benefit)	**8,367**	**(1,333,772)**
Current tax payable	**-**	**3,071**

6: DISCONTINUED OPERATIONS

As set out in Note 6 of the financial report of Probiotec Limited for the year ended 30 June 2011 ("2011 Financial Report"), Probiotec Limited undertook a comprehensive strategic and operational review of its business operations, assets and financial position. Full details of each of the operations classifed as discontinued can be found in Note 6 of the 2011 Financial Report, subject to the following updates:

China operations

Following further assessment of the performance of Hangzhou Probiotec Trading Co Ltd, the Group's Chinese incorporated entity, the directors have decided to divest this entity in full. This divestment will be in the form of a buy-out by the current Chinese management team for a nominal fee. This divestment was completed on 29 February 2012.

Brand discontinuance

In 2009, the Group commenced the sale of vitamins, supplements and consumer health products in Europe under the Bioremedies brand. Unfortunately, sales of this brand have failed to increase to a level that achieves profitability and as a result, the Group will discontinue all operations, including manufacturing, sales and marketing activities.

Hong Kong operations

In 2009, the Company established a Hong Kong subsidiary named Probiotec (Hong Kong) Limited. The purpose of this entity was to market and distribute the Company's weight loss and pharmaceutical products in Hong Kong. Since incorporation, Probiotec (Hong Kong) Limited has failed to expand its revenue and market share to a level that achieves profitability. Following the strategic review, it was determined that this operation did not show a reasonable probability of achieving acceptable returns in the future and as a result it was decided that this operation would be discontinued.

Manufacturing site: Bundaberg, QLD

Probiotec operates a manufacturing site in Bundaberg, QLD that produces a range of ingredients for use primarily in animal nutrition applications. As a result of the strategic review, it was decided that this operation was not consisitent with the Company's core business strategy and did not provide sufficient returns.

The Comprehensive income of the discontinued operations was:	2012 $	2011 $
Revenue	418,814	1,713,753
Impairment and reclassification costs	(1,378,193)	(2,699,980)
Expenses	(20,491)	(8,948,307)
Loss from discontinued operations before income tax	(979,870)	(9,934,534)
Income tax benefit / (expense)	-	1,679,396
Loss from discontinued operations after income tax	(979,870)	(8,255,138)
The cash flow of the discontinued operations was:		
Net cash flow used in operating actvities	(347,606)	(770,985)
Net cash flow used in investing actvities	-	(121,985)
Net cash flow used in financing activities	-	-
Net decrease in cash held	(347,606)	(892,970)

7: CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that may have a financial impact on the entity and that are believed to be reasonable under the circumstances.
(a) The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

(i) Value in use calculation assumptions

The recoverable amount of each cash-generating unit used for impairment testing is determined based on value-in-use calculations. Value-in-use is calculated based on the present value of cash flow projections over a 5-year period. The discounted cash flows for each cash-generating unit is calculated based on management forecasts for sales, gross profit and resultant earnings. The assumed growth rate beyond the forecast cash flow period and discount rate used in the determination of value in use were 5% and 12.4% respectively. The discounted rate used is the Weighted Average Cost of Capital (WACC) of the Group at the reporting date. These value-in-use calculations are sensitive to changes in the key assumptions used. Changes in the nature or quantum of key assumptions would alter the value-in-use calculations and could potentially result in certain cash-generating units being subject to impairment.

(ii) Amortisation of intangibles

As detailed in Note 1 (j), the group has a policy of amortising intangible assets with a finite useful life over a period of 10 to 40 years (other than those which are subject to a fixed term license) and the remainder have been determined to have an indefinite useful life. The carrying value of those assets with a finite useful life is $18,589,211 and those with an indefinite useful life is $9,743,751 (refer to Note 18). The determination of the useful life of each intangible asset, which comprises capitalised product development costs, is based on the group's knowledge of each major category of intangible assets and the future economic benefits expected to be received from each. The group reassesses the useful life of intangible assets at each reporting date and at any future period may change the useful life of an intangible asset based on information available at that date. The group recognised amortisation of $694,327 relating to assets with a finite useful life during the current year.

NOTES TO THE FINANCIAL STATEMENTS (continued)

8: KEY MANAGEMENT PERSONNEL AND THEIR RELATED PARTIES DISCLOSURES

Full details of Key Management Personnel and their related party disclosures are set out in the Remuneration Report section of the Directors Report.

(a) Key management personnel compensation:

	2012 $	2011 $
Short-term employee benefits	1,801,518	2,092,825
Post-employment benefits	261,232	270,087
Termination benefits	-	-
Share-based payments	-	37,658
Total compensation	2,062,750	2,400,570

(b) The number of options[1] held by directors and key management personnel for the year ended 30 June 2012 is as follows:

	Balance at start of the year number	Granted as compensation during the year number	Exercised during the year number	Forfeited / Lapsed during the year number	Balance at end of the year number	Balance vested and exercisable at end of the year number	Balance unvested and/or unexerceseable at end of the year number
Maurice Van Ryn	-	-	-	-	-	-	-
Richard David Kuo	-	-	-	-	-	-	-
Graham Henry Buckeridge	-	-	-	-	-	-	-
Robert Maxwell Johnston	-	-	-	-	-	-	-
Charles Wayne Stringer	2,200,000	-	-	(700,000)	1,500,000	-	1,500,000
Wesley Stringer	135,000	-	-	(25,000)	110,000	-	110,000
Dustin Stringer	120,000	-	-	(20,000)	100,000	-	100,000
Mark Chatfield	75,000	-	-	(25,000)	50,000	-	50,000
Humera Ahmad	60,000	-	-	(25,000)	35,000	-	35,000
Scott Patterson	-	-	-	-	-	-	-
Jared Stringer	95,000	-	-	(20,000)	75,000	-	75,000
	2,685,000	**-**	**-**	**(815,000)**	**1,870,000**	**-**	**1,870,000**

**The executives have no access to the shares until expiry of 36 months of their employment with the company or an Associated Body Corporate from the date of grant of the shares. All shares are forfeited if the grantee resigns from the company prior to the expiry of 36 from the date of grant of the shares.*

Option[1] Holdings of Key Management Personnel for the year ended 30 June 2011:

	Balance at start of the year number	Granted as compensation during the year number	Exercised during the year number	Forfeited/ Lapsed during the year number	Balance at end of the year number	Balance vested and exercisable at end of the year number	Balance unvested at end of the year number
Maurice Van Ryn	-	-	-	-	-	-	-
Richard David Kuo	-	-	-	-	-	-	-
Graham Henry Buckeridge	-	-	-	-	-	-	-
Robert Maxwell Johnston	-	-	-	-	-	-	-
Charles Wayne Stringer	2,600,000	-	-	400,000	2,200,000	1,000,000	1,200,000
Wesley Stringer	272,503	-	-	137,503	135,000	75,000	60,000
Dustin Stringer	195,001	-	-	75,001	120,000	60,000	60,000
Mark Chatfield	175,003	-	-	100,003	75,000	50,000	25,000
Humera Ahmad	125,001	-	-	65,001	60,000	45,000	15,000
Alan Hong	160,002	-	-	100,002	60,000	45,000	15,000
Matthew Dalton	180,001	-	-	50,001	130,000	70,000	60,000
David Erasmus	90,000	-	-	-	90,000	65,000	25,000
Jared Stringer	157,501	-	-	62,501	95,000	50,000	45,000
	3,955,012	**-**	**-**	**990,012**	**2,965,000**	**1,460,000**	**1,505,000**

NOTES TO THE FINANCIAL STATEMENTS (continued)

Ordinary share holdings of Key Management Personnel

	Balance at 1/07/2010	Share acquisitions through exercise of share options	CEO Options Exercised	Other purchases during the year*	Sold during the year	Balance at 30/06/11	Share acquisitions through exercise of share options	CEO Options Exercised	Other purchases during the year*	Sold during the year	Balance at 30/06/12
Directors											
Maurice Van Ryn	187,502	-	-	93,599	-	281,101	-	-	525,000	-	806,101
Charles Wayne Stringer	7,340,954	-	-	487,689	-	7,828,643	-	-	529,209	-	8,357,852
Wes Stringer	272,811	-	-	-	-	272,811	-	-	287,934	-	560,745
Graham Harry Buckeridge	1,348,684	-	-	-	-	1,348,684	-	-	-	-	1,348,684
Robert Maxwell Johnston	15,500	-	-	187,500	-	203,000	-	-	31,000	-	234,000
Richard David Kuo	73,459	-	-	1,267	-	74,726	-	-	-	-	74,726
Total for Directors	9,238,910	-	-	770,055	-	10,008,965	-	-	1,373,143	-	11,382,108
Key Executive Personnel											
Scott Patterson	-	-	-	-	-	-	-	-	-	-	-
Jared Stringer	90,164	-	-	1,446	-	91,610	-	-	47,107	-	138,717
Mark Chatfield	-	-	-	-	-	-	-	-	-	-	-
Dustin Stringer	82,700	-	-	15,300	-	98,000	-	-	-	(21,000)	77,000
Humera Ahmad	-	-	-	-	-	-	-	-	-	-	-
Total for Key Executive Personnel	172,864	-	-	16,746	-	189,610	-	-	47,107	(21,000)	215,717

** Includes on market purchases and dividend reinvestment plan allotments.*

[1] The term Option includes unvested fully paid ordinary shares issues and the associated loans with recourse to the shares which are issued under the Probiotec Limited Employee Share Plan (ESP). These shares and loans together have substantially similar financial and economic dynamics to options. Other than the options issued to Wayne Stringer, all other "options" referred to in this table are shares and associated loans issued under the ESP.

9: REMUNERATION OF AUDITORS

	2012 $	2011 $
Amounts paid/payable to Moore Stephens Melbourne for:		
Audit services		
Auditing or reviewing the financial report	90,000	-
	90,000	-
Amounts paid/payable to BDO Audit (NSW-VIC) Pty Ltd for:		
Audit services		
Auditing or reviewing the financial report	-	96,163
	-	96,163
Amounts paid/payable to related practices of BDO Audit (NSW-VIC) Pty Ltd for:		
General advice and services from BDO Ireland	-	26,701
General advice and services from BDO LLP	-	4,234
	-	30,935

10: DIVIDENDS

No dividend has been declared or paid in relation to the financial years ended 30 June 2011 or 30 June 2012

	2012 Cents per Share	Total $	2011 Cents per Share	Total $
Recognised Amounts				
Fully Paid Ordinary Shares				
Interim dividend for half year ended 31 December fully franked at 30% corporate tax rate	-	-	-	-
Unrecognised Amounts				
Fully paid ordinary shares				
Final dividend for year ended 30 June, fully franked at 30% corporate tax rate	-	-	-	-

	2012 $	2011 $
Dividend franking account		
Amount of franking credits available for subsequent years	1,157,405	1,039,753

11: CASH AND CASH EQUIVALENTS

Cash on hand and at bank	193,388	938,107

Interest rate risk exposure

The Group's and the parent entity's exposure to interest rate risk is discussed in note 34.

12. TRADE AND OTHER RECEIVABLES

	2012 $	2011 $
CURRENT		
Trade accounts receivable - third parties	7,956,963	8,846,118
Less: allowance for impairment of receivables	(221,538)	(218,401)
Total current trade receivables	7,735,425	8,627,717
GST receivable	-	845,171
Other receivables	711,490	777,417
Total current trade and other receivables	**8,446,915**	**10,250,305**

(a) An analysis of trade receivables that are past due but not impaired at the reporting date:

	2012 Gross $	2012 Allowance $	2011 Gross $	2011 Allowance $
Not past due	6,954,482	-	7,847,260	-
Past due 1 - 30 days	511,179	-	455,502	-
Past due 31 - 60 days	200,518	-	268,299	-
Past 61 days	290,784	(221,538)	275,057	(218,401)
	7,956,963	**(221,538)**	**8,846,118**	**(218,401)**

(b) Impaired trade receivables

Trade debtors are generally extended on credit terms of between 14 days to 60 days. As at 30 June 2012, current trade receivables of the Group with a nominal value of $290,784 (2011 - 275,057) were impaired. The amount of the allowance was $221,538 (2011 - $218,401). The individually impaired receivables mainly relate to customers, which are in unexpectedly difficult economic situations.

Trade receivables that are neither past due or impaired relate to long standing customers with a good payment history.

Other receivables are expected to be recoverable in full and are due from reputable companies.

Movements in the provision for impairment of receivables are as follows:

	2012 $	2011 $
At 1 July	**218,401**	**323,511**
Provision for impairment recognised during the year	47,056	242,390
Receivables written off during the year as uncollectible	(43,919)	(347,500)
At 30 June	221,538	218,401

Payment terms on receivables past due but not considered impaired have not been renegotiated. The Group has been in direct contact with the relevant customers and are reasonably satisfied that payment will be received in full.

(c) Fair value and credit risk

Due to the short term nature of these receivables, their carrying value is assumed to approximate their fair value.

(d) Foreign exchange and interest rate risk

Information about the Group's and the parent entity's exposure to foreign currency risk and interest rate risk in relation to trade and other receivables is provided in note 34.

	2012 $	2011 $
13: INVENTORIES		
CURRENT		
Raw material - at cost	6,814,753	7,429,608
Work in progress - at cost	978,095	1,426,772
Finished goods - at cost	6,460,769	5,956,881
	14,253,617	**14,813,261**
14: OTHER CURRENT ASSETS		
Prepayments	489,770	415,305

15: INTERESTS IN JOINT VENTURE ENTITIES

(a) During the year, Interests were held in the following joint venture company:

Name	Domicile	Ownership Interest 2012	Ownership Interest 2011
Probiotec BLC Pty Limited ("PBLC")	Australia	100%	50%

PBLC is a joint venture entity between Probiotec Limited and SP Health Co Pty Ltd and is involved in the marketing and distribution of a range of health products. The reporting date is 30 June 2012. As set out in Note 32, on 15 September 2011 Probiotec Limited acquired the 50% of PBLC that it previously did not own. Prior to this acquisition, PBLC was accounted for using the proportionate consolidation method.

NOTES TO THE FINANCIAL STATEMENTS (continued)

16: LOANS RECEIVABLE

	2012 $	2011 $
Loans receivable	-	**596,817**

Loans receivable are due from commercial partners with which the Group has a long standing relationship. All loans receivable are secured by a fixed and floating charge over the assets of the commercial partner and are supported by a directors guarantee.

17: PROPERTY, PLANT AND EQUIPMENT

	2012 $	2011 $
Freehold land - at valuation	3,910,000	4,337,775
Building - at independent valuation	12,390,000	16,129,560
Less: Accumulated depreciation	-	(2,364,164)
	12,390,000	**13,765,396**
Plant & equipment - at cost	38,654,058	41,368,655
Less: Accumulated depreciation	(11,996,957)	(15,663,975)
	26,657,101	**25,704,680**
Leased plant & equipment	6,648,812	6,200,358
Less: Accumulated depreciation	(1,667,450)	(1,424,616)
	4,981,362	4,775,742
TOTAL PROPERTY, PLANT AND EQUIPMENT	**47,938,462**	**48,583,593**

All of the Group's freehold land and buildings were revalued by an independent valuer in June 2012 and resulted in a net revaluation decrease of $109,213. Valuations were made on the basis of weighted depreciated values and open market values. The revaluation deficit net of applicable deferred income taxes was credited to an asset revaluation reserve in shareholders' equity. As at 30 June 2012, if the cost model had been applied, the carrying value of the Group's freehold land and buildings would have been $3,106,480 and $8,976,371 respectively.

Movements during the year	Freehold land $	Buildings $	Plant, Equipment & Other $	Leased Plant, Equipment & Other $	Total $
Consolidated Group					
Carrying amount at 1 July 2010	4,337,775	14,410,578	27,810,164	5,623,361	52,181,878
Additions	-	-	1,924,418	277,123	2,201,541
Acquisitions through business combinations	-	-	(2,041,031)	-	(2,041,031)
Reclassification	-	-	716,549	(716,549)	-
Disposals	-	-	(179,224)	(13,355)	(192,579)
Depreciation and amortisation	-	(645,182)	(2,526,196)	(394,838)	(3,566,216)
Carrying amount at 30 June 2011	4,337,775	13,765,396	25,704,680	4,775,742	48,583,593
Carrying amount at 1 July 2011	4,337,775	13,765,396	25,704,680	4,775,742	48,583,594
Additions	-	37,229	3,383,724	711,123	4,132,076
Impairment	-	-	-	-	-
Revaluation	165,600	(274,813)	-	-	(109,213)
Reclassification	-	(75,591)	-	-	(75,591)
Disposals	(593,375)	(421,575)	(336,480)	(111,783)	(1,463,213)
Depreciation and amortisation	-	(640,646)	(2,094,824)	(393,720)	(3,129,190)
Carrying amount at 30 June 2012	3,910,000	12,390,000	26,657,100	4,981,362	47,938,462

18. INTANGIBLE ASSETS

	2012 $	2011 $
(a) Intangible summary and reconciliation		
Acquired intangible assets - indefinite life:		
Goodwill - at cost	2,079,000	2,079,000
Developed products - at cost	3,785,739	6,912,634
	5,864,739	**8,991,634**
Acquired intangible assets - finite life:		
Developed products - at cost	12,229,190	11,729,541
Accumulated amortisation	(552,005)	(243,606)
	11,677,185	**11,485,935**
Capitalised development costs - indefinite life:		
Developed products - at cost	2,789,600	2,678,194
Products under development - at cost	1,089,412	1,360,555
	3,879,012	**4,038,749**
Capitalised development costs - finite life:		
Developed products - at cost	7,564,624	5,309,205
Accumulated amortisation	(652,598)	(266,670)
	6,912,026	5,042,535
Total intangible assets	**28,332,961**	**29,558,853**

Probiotec Ltd has both acquired and capitalised trademarks, licenses, product development costs and product dossiers ("Developed Products"). Product dossiers incorporate formulations, registrations, Therapeutic Goods Administration (TGA) listings, stability and validation data, and manufacturing and testing procedures.

Reconciliation of Intangible Assets:

	Goodwill	Developed Products	Products under Development	Total
Opening balance as at 1 July 2010	5,444,527	25,332,990	946,543	31,724,059
Impairment	(3,365,527)	(408,949)	-	(3,774,476)
Additions	-	-	1,933,653	1,933,653
Transfer of commercialised product	-	1,519,641	(1,519,641)	-
Amortisation	-	(324,384)	-	(324,384)
Closing balance as at 30 June 2011	**2,079,000**	**26,119,298**	**1,360,555**	**29,558,853**
Opening balance as at 1 July 2011	2,079,000	26,119,298	1,360,555	29,558,853
Acquisitions	-	499,649	-	499,649
Additions	-	806,074	1,290,852	2,096,926
Transfer of commercialised product	-	1,561,995	(1,561,995)	-
Disposals *	-	(3,126,895)	-	(3,126,895)
Impairment	-	(1,245)	-	(1,245)
Amortisation	-	(694,327)	-	(694,327)
Closing balance as at 30 June 2012	**2,079,000**	**25,164,549**	**1,089,412**	**28,332,961**

'* On 5 December 2011, the Company announced the sale of the Milton brand, including all intellectual property and business assets associated with this brand for all the countries it has the rights for, comprising Australia, New Zealandand several other South East Asian countries. The sale price of $6 million resulted in a one-off item of other income (see Note 2 for details) and a reduction in intangible assets of $3,126,895 (being the intangible asset balance applicable to the Milton brand).

Estimated useful life of intangible assets

Intangible assets, comprising Developed Products and goodwill, have indefinite useful lives apart from Developed Products which are subject to a license with a specified term. Developed Products with a finite life have a term of 10 to 40 years. Developed Products with indefinite lives comprise trademarks and product dossiers. Developed Products with finite useful lives are amortised on a straight line basis over their effective life. The current amortisation charges for intangible assets are included under depreciation and amortisation expense in the income statement. The directors consider intangibles to have an indefinite life when, based on an analysis of all relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate net cashflows for the group.

Goodwill

	2012 $	2011 $
Breakdown of goodwill at year end:		
Australian Dairy Proteins Pty Ltd	2,079,000	2,079,000
	2,079,000	2,079,000

Impairment of Intangibles

Developed products

As at 30 June 2012, impairment charges in the amount of $1,245 were incurred in relation to developed products which no longer generate future cash flows sufficient to justify their carrying value. The impairment charge has been disclosed in loss from discontinued operations in the statement of comprehensive income.

Impairment Disclosures

Goodwill is tested annually for impairment, based on value-in-use calculations conducted using the assumptions outlined in note 7.

The amount of goodwill and intangible assets with indefinite useful lives allocated to each cash-generating unit for the purposes of annual impairment testing are:

	Pharmaceuticals and consumer healtth	Contract manufacturing	Nutritional products	Export sales	Research and development	Total
Year ended 30 June 2012						
Goodwill	2,079,000	-	-	-	-	2,079,000
Intangibles with indefinite useful lives	6,420,949	-	100,130	1,143,672	-	7,664,751
Year ended 30 June 2011						
Goodwill	2,079,000	-	-	-	-	2,079,000
Intangibles with indefinite useful lives	9,807,711	-	-	1,143,672	-	10,951,383

The discount rates used to determine the value-in-use are:	2012 $	2011 $
Probiotec BLC Pty Ltd	12.4%	n/a
Australian Dairy Proteins Pty Ltd	12.4%	13.8%
Intangibles with indefinite useful lives	12.4%	13.8%

	2012 $	2011 $
19: DEFERRED TAX ASSETS		
Deferred tax assets is comprised as follows:		
Temporary differences - provisions	461,050	399,384
Temporary differences - Property, plant & equipment	166,145	580,475
Temporary differences - leases	829,030	813,860
Temporary differences - other	168,765	203,637
Offset against deferred tax liabilities	(2,950,521)	(2,390,115)
Tax losses	2,835,810	1,798,274
	1,510,279	**1,405,515**
20: TRADE AND OTHER PAYABLES		
Trade accounts payable	7,511,362	7,657,040
Sundry creditors & accruals	2,164,986	2,533,864
GST payable	537,374	1,280,886
	10,213,722	**11,471,790**

(a) Fair value

Due to the short term nature of these payables, their carrying value is assumed to approximate their fair value.

(b) Foreign exchange risk

Amounts payable in foreign currencies	2012 $	2011 $
Current		
Euro	200,388	150,473
Great British Pounds	161,465	362,945
US Dollars	764	53,592
NZD	1,121	9,515
HKD	-	90,289
CNY	-	131,487
	363,738	**798,301**

Detailed information about the Group's and the parent entity's exposure to foreign currency risk in relation to trade and other payables is provided in note 34.

	2012 $	2011 $
21: INTEREST-BEARING LIABILITIES		
Current		
Secured borrowings		
Bank loans	20,915,968	26,341,358
Lease liabilities	863,448	836,782
	21,779,416	**27,178,140**
Non-Current		
Secured borrowings		
Bank loans	150,000	250,000
Lease liabilities	1,899,986	1,876,086
	2,049,986	**2,126,086**
(a) Total current and non-current secured liabilities:		
Bank loans	21,065,968	26,591,358
Lease liabilities	2,763,434	2,712,868
	23,829,402	**29,304,226**
(b) The carrying amount of the assets secured by a first registered mortgage:		
Freehold land and building (Note 16)	16,300,000	18,103,171

(c) The bank loans are provided by Rabo Australia Limited and are secured by a registered first mortgage over certain freehold property of the parent entity and the subsidiaries which has a carrying amount of $16,300,000 at 30 June 2012.

The bank covenants require tangible net worth to exceed $35 million, an equity ratio of greater than 50%, debt service to EBITDA to exceed 1.5 and the ratio of financial indebtedness to EBITDA of less than 3 as at 30 June 2012, where EBITDA excludes extraordinary and/or non-cash events. The Group is in compliance with the bank convenants.

The bank loans provided by Commonwealth Bank and Rabo Australia Limited are secured by cross guarantees between Probiotec Limited and its controlled entities.

(d) Finance lease liabilities:

Weighed average interest rate of 7.77%

Secured by leased plant / assets

(e) Interest rate risk exposure

The Group's and the parent entity's exposure to interest rate risk is discussed in note 34.

	2012 $	2011 $
22: PROVISIONS		
Current		
Leave entitlements (a)	969,210	894,791
Non-Current		
Leave entitlements (a)	348,006	280,993
Total provisions	**1,317,216**	**1,175,784**

(a) Provision for leave entitlements represents accrued annual leave along with an allowance for long service leave either earned by employees and not yet taken or partly earned. For partly earned long service leave, historical retention rates are used to determine likelihood of achieving fully vested long service leave.

23: DEFERRED TAXES

	2012 $	2011 $
Deferred taxes is comprised as follows:		
Deferred tax assets (note 19)	1,510,279	1,405,515
Deferred tax liabilities - temporary differences (a)	(3,330,902)	(3,291,532)
Net deferred tax liabilities	**(1,820,623)**	**(1,886,017)**
Deferred tax expense debit / (credit) to income tax expense	**8,367**	**(1,330,386)**
Deferred tax expense charged to equity	**73,761**	**-**
(a) Deferred tax liabilities comprises:		
Temporary differences - property, plant & equipment	(1,494,409)	(2,811,727)
Temporary differences - capitalised development costs	(2,891,322)	(2,313,064)
Temporary differences - other	1,054,829	1,833,259
	(3,330,902)	**(3,291,532)**

Reconciliation of net deferred tax liabilities:	
Opening as at 1 July 2010	(3,216,403)
Less : deferred tax expense charge (credit) to income	1,330,386
Less : deferred tax expense charged to equity	-
Closing as at 30 June 2011	(1,886,017)
Less : deferred tax benefit	(8,367)
Less : deferred tax expense charged to equity	73,761
Closing as at 30 June 2012	**(1,820,623)**

	2012 $	2011 $
24: CONTRIBUTED EQUITY		
52,929,356 (2011: 52,929,356) fully paid ordinary shares	35,072,269	36,581,517
Reconciliation of fully paid ordinary shares		
Balance at beginning of the financial year	36,581,517	36,360,891
Issue of shares	-	220,626
Cancellation of shares held under Equity Compensation Plan (see Note 25)	(1,509,248)	-
Equity raising expenses	-	-
Balance at end of financial year	**35,072,269**	**36,581,517**

	2012 No,	2011 No,
Reconciliation of ordinary shares		
Balance at the beginning of reporting period	52,929,356	52,779,127
Shares issued during the year	-	150,229
Balance at end of the report date	**52,929,356**	**52,929,356**

Ordinary shares participate in dividends and the proceeds on winding up of the parent entity in proportion to the numbers of shares.

At the shareholders meeting each ordinary share is entitled to one vote when a poll is called, otherwise each shareholders has one vote on a show of hands.

(a) Capital management

The Group's objective is to maintain a strong capital base to ensure the Group continues as a going concern as well as to maintain optimal returns to shareholders and benefits for other stakeholders. Management also aims to maintain an optimal capital structure to reduce the cost of capital.

The Group's debt and capital includes ordinary share capital and financial liabilities, supported by financial assets. The Group is not subject to externally imposed capital requirements.

The Group effectively manages the Group's capital by monitoring its gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings less cash and cash equivalents. Total capital is calculated as 'equity' as shown in the balance sheet plus net debt.

The level of gearing in the Group is periodically reviewed by the Board to ensure that a responsible level of gearing is maintained. The directors consider that the Group is currently operating at a responsible gearing level. The gearing ratios at 30 June 2012 and 30 June 2011 were as follows:

	2012 $	2011 $
Total borrowings	23,829,402	29,304,226
Less cash and cash equivalents	(193,388)	(938,107)
Net debt	23,636,014	28,366,119
Total contributed equity (less shares held by Equity Compensation Plan)	33,686,518	33,686,519
Total capital employed	**57,322,532**	**62,052,639**
Gearing ratio	41.2%	45.7%

There were no changes to the Group's approach to capital management from 2011.

NOTES TO THE FINANCIAL STATEMENTS (continued)

	2012 $	2011 $
25: SHARES HELD BY EQUITY COMPENSATION PLAN		
Balance at beginning of report period	(2,894,998)	(2,894,998)
Employee share plan issue	-	-
Employee share plan forefeiture / expiry	1,509,248	-
Employee share plan payments	-	-
Balance at the end of the reporting period	**(1,385,750)**	**(2,894,998)**

Reconciliation of shares held by equity compensation plan:	No.	No.
Opening balance	2,142,517	2,142,517
Shares issued	-	-
Shares forfeited / expired	(1,442,517)	-
Shares sold	-	-
Closing Balance	**700,000**	**2,142,517**

The shares held in the "Equity Compensation" account is used to record the balance of Probiotec Limited ordinary shares which as at the end of the financial period have not vested to Group employees, and are therefore controlled by the Group. 700,000 (2011: 2,142,517) shares have been issued and are held by the Probiotec Limited Employee Share Plan (ESP).

	2012 $	2011 $
26: RESERVES		
Asset revaluation reserve	4,217,149	4,523,385
Foreign currency translation reserve	(658,425)	(681,306)
Reconciliation of foreign currency translation reserve		
Balance at beginning of financial year	(681,306)	284,073
Translation of net investment in foreign entities	(362,886)	(965,379)
Impairment of net investment in foreign entities	385,767	-
Balance at end of financial year	**(658,425)**	**(681,306)**

Asset revaluation reserves arise on the revaluation of non-current assets.

Where a revalued asset is sold that portion of the reserve which relates to that asset, and is effectively realised, is transferred to retained earnings.

Foreign currency translation reserves arise upon the translation of net investments in foreign entities at balance date.

27: COMMITMENTS

	2012 $	2011 $
Lease commitments		
Operating leases		
Non-cancellable operating leases contracted for but not capitalised in the financial statement.		
Payable - minimum lease payments:		
Within one year	406,991	245,721
Later than one year but not later than 5 years	659,969	256,082
Commitments not recognised in the statement of financial position	1,066,960	501,803
Finance leases commitments		
Payable - minimum lease payments:		
Within one year	1,026,150	838,279
Later than one year but not later than 5 years	2,020,602	2,243,326
Minimum lease payments	3,046,752	3,081,606
Less: Future finance charges	(283,318)	(368,737)
	2,763,434	**2,712,868**
Representing lease liabilities (Note 21):		
Current	863,448	836,782
Non-current	1,899,986	1,876,086
	2,763,434	**2,712,868**

The weighted average interest rate implicit in the leases is 7.77%. The carrying value of assets purchased via leases is $4,981,362 (2011: $4,775,742)

Leases are entered into with terms between 3 to 5 years. Leased property is held at all of the group's Australian based manufacturing sites. Leases may be renewed by negotiation. No contingent rents are payable under any lease contract entered into. The group also entered into a lease for the rental of its manufacturing site in Dundalk, Ireland. This is a 20 year lease with a right for the group to terminate at any time after the expiry of the third year of the lease without penalty.

The Group has also entered into contracts relating to the relocation, upgrade and construction of its ADP protein extraction plant. As at reporting date, these contracts have a balance of $3,869,989 to be paid. These contracts are all expected to be completed within the next 12 months and funding for these amounts is by way of finance facilities with the Group's current lenders, which were approved and in place at balance date.

28. SHARE BASED PAYMENTS

(a) Incentive Option Scheme

The Group has in place an option incentive scheme to encourage employees to share in the ownership of the company in order to promote the long-term success of the company as a goal shared by the employees. This scheme is designed to attract, motivate and retain eligible employees. These options are governed by the Probiotec Limited Employee Share Plan ("the plan"). Under the plan, participants may be granted options which vest if the participant remains in the employment of the group for a period of three years from the grant date. Participation in the plan is at the Board's discretion and no individual has a contractual right to participate in the plan or to receive any guaranteed amount of options. For details of options issued to key management personnel refer to the remuneration report.

CEO Employment Options for the year ended 30 June 2012

Grant Date	Vesting date	Expiry date	Exercise price ($)	Balance at start of year number	Options granted number	Options forfeited/ exercised number	Balance at end of year number	Vested and exercisable at end of year
05.08.2008	30.06.2010	30.06.2013	1.50	500,000	-	-	500,000	-
05.08.2008	30.06.2011	30.06.2013	1.75	500,000	-	-	500,000	-
05.08.2008	30.06.2012	30.06.2013	2.00	500,000	-	-	500,000	-
01.07.2009	30.06.2012	30.06.2012	1.00	300,000	-	(300,000)	-	-
01.07.2009	30.06.2012	30.06.2012	1.00	400,000	-	(400,000)	-	-
				2,200,000	-	(700,000)	1,500,000	-
Weighted average exercise price				$1.51	$-	$1.00	$1.75	$-

The weighted average contractual life remaining on CEO options outstanding is 365 days as at balance date.

CEO Employment Options for the year ended 30 June 2011

Grant Date	Vesting date	Expiry date	Exercise price ($)	Balance at start of year number	Options granted number	Options forfeited/ exercised number	Balance at end of year number	Vested and exercisable at end of year
05.08.2008	30.06.2010	30.06.2013	1.50	500,000	-	-	500,000	500,000
05.08.2008	30.06.2011	30.06.2013	1.75	500,000	-	-	500,000	500,000
05.08.2008	30.06.2012	30.06.2013	2.00	500,000	-	-	500,000	-
01.07.2008	30.06.2010	30.06.2011	1.00	400,000	-	(400,000)	-	-
01.07.2009	30.06.2012	30.06.2012	1.00	300,000	-	-	300,000	-
01.07.2009	30.06.2012	30.06.2012	1.00	400,000	-	-	400,000	-
				2,600,000	-	(400,000)	2,200,000	1,000,000
Weighted average exercise price				$1.31	$-	$-	$1.51	$1.63

Employee incentive scheme options for the year ended 30 June 2012

The following incentive scheme options were issued to eligible employees:

Grant Date	Vesting date	Expiry date	Exercise price ($)	Balance at start of year number	Options granted during the year number	Options exercised/ lapsed during the year number	Balance at end of year number	Vested and exercisable at end of year
01.07.2007	30.06.2010	30.06.2012	1.50	240,000	-	(240,000)	-	-
01.07.2008	30.06.2011	30.06.2013	1.50	305,000	-		305,000	-
30.06.2009	30.06.2012	30.06.2014	2.35	385,000	-		385,000	-
01.07.2007	30.06.2010	30.06.2012	0.80	50,000	-	(50,000)	-	-
01.07.2009	30.06.2012	30.06.2014	2.35	10,000	-		10,000	-
				990,000	-	(290,000)	700,000	-
Weighted average exercise price				$1.35	$-	$1.38	$1.98	$-

Employee incentive scheme options for the year ended 30 June 2011

The following incentive scheme options were issued to eligible employees:

Grant Date	Vesting date	Expiry date	Exercise price ($)	Balance at start of year number	Options granted during the year number	Options exercised/ lapsed during the year number	Balance at end of year number	Vested and exercisable at end of year
30.06.2006	30.06.2009	30.06.2011	0.80	927,517	-	(927,517)	-	-
01.07.2007	30.06.2010	30.06.2012	1.50	240,000	-	-	240,000	240,000
01.07.2008	30.06.2011	30.06.2013	1.50	325,000	-	(20,000)	305,000	305,000
30.06.2009	30.06.2012	30.06.2014	2.35	420,000	-	(35,000)	385,000	-
01.07.2007	30.06.2010	30.06.2012	0.80	50,000	-	-	50,000	50,000
05.08.2008	05.08.2011	05.08.2013	1.50	70,000	-	(70,000)	-	-
05.08.2008	06.05.2011	06.05.2013	1.50	100,000	-	(100,000)	-	-
01.07.2009	30.06.2012	30.06.2014	2.35	10,000	-	-	10,000	-
				2,142,517	-	(1,152,517)	990,000	595,000
Weighted average exercise price				$1.35	$-	$0.96	$1.35	$1.16

[1]The term Option includes unvested fully paid ordinary shares issues and the associated loans with recourse to the shares which are issued under the Probiotec Limited Employee Share Plan (ESP). These shares and loans together have substantially similar financial and economic dynamics to options. Other than the options issued to Wayne Stringer, all other "options" referred to in this note are shares and associated loans issued under the ESP.

The weighted average contractual life remaining on employee incentive scheme options outstanding is 579 days as at balance date.

The fair value at grant date of the options issued as part of the employee incentive scheme were calculated internally using the Black Scholes pricing model that takes into account the term of the option, the underlying value of the shares, the exercise price, the expected dividend yield, the impact of dilution and the risk-free interest rate.

NOTES TO THE FINANCIAL STATEMENTS (continued)

The inputs used in the valuation of these options were:

Exercise price:	as per table above.
Expected volatility of company shares:	42% for options granted on 30.06.2006, 38% for options granted on 01.07.2007 and 01.07.2008, 48% for options granted on 30.06.2009 and 01.07.2009.
Risk-free interest rate:	5.7% for options issued on 30.06.2006, 01.07.2007 and 01.07.2008, 5% for options issued on 30.06.2009 and 01.07.2009.
Vesting period:	3 years
Projected dividend yield:	4%
Share price:	weighted average share price for 5 trading days preceeding grant date.

For options issued prior to 30 June 2008, the expected volatility during the term of the options was based around assessments of the volatility of similar-sized listed entities and entities in similar industries. For options issued after 30 June 2008, the volatility during the term of the options was calculated from the standard deviation of day to day logarithmic historical price changes. The value of the options has been expensed to remuneration on a proportionate basis over the period from the grant date to the vesting date.

(b) Expenses arising from share-based payments

	2012 $	2011 $
Options issued under incentive option scheme	-	38,892
Options issued to CEO	-	9,415
	-	**48,307**

29: RELATED PARTY TRANSACTIONS AND BALANCES

Transactions between related parties are on normal commercial terms and conditions no favourable than those available to other parties unless otherwise stated. No balances have been written off and no provision for doubtful debts has been made against any balances with related parties.

Associated companies

Payments were made to Pier Capital Pty Ltd, an entity associated with Mr Richard Kuo (director). These payments were for the provision of financial modelling services performed	-	35,000

Key Management personnel

There were no transactions between Key Management Personell and Probiotec Limited or any of its subsidiaries during the year ended 30 June 2012 other than as disclosed in note 7.

Identification of Related Parties - Ultimate Parent Entity

The ultimate parent company is Probiotec Limited which is incorporated in Australia.

30: NOTES TO THE STATEMENT OF CASH FLOWS

	2012 $	2011 $
(a) Financing facilities with banks		
Secured bank overdraft facility:		
Facility balance	1,500,000	500,000
Amount used	-	-
Amount unused	1,500,000	500,000
Secured term loan and working capital facilities with banks:		
Facility balance	26,147,500	33,224,040
Amount used	(21,065,968)	(26,591,358)
Amount unused	5,081,532	6,632,682
Lease finance facilities:		
Facility balance	12,000,000	12,000,000
Amount used	(2,763,434)	(2,712,868)
Amount unused	9,236,566	9,287,132
Bank bill acceptance facility, reviewed annually:		
Facility balance	250,000	350,000
Amount used	(250,000)	(350,000)
Amount unused	-	-
(b) Reconciliation of Profit from Ordinary Activities After Related Income Tax to Net Cash Flows From Operating Activities:		
Profit after related income tax	1,249,380	(10,337,787)
Depreciation and amortisation	3,824,259	3,890,600
Loss (profit) on sale of plant and equipment	(486,447)	3,195
Profit on sale of intangible assets	(2,856,205)	-
Impairment and reclassification costs	1,378,193	5,815,507
Equity translation	(669,122)	(965,379)
(Decrease)/increase in net deferred taxes	(65,394)	(1,330,386)
(Increase)/decrease in inventories	559,644	7,670,971
(Increase)/decrease in trade and other receivables	1,803,391	1,766,307
(Increase)/decrease in other current assets	(74,465)	(26,301)
Increase/(decrease) in trade and other payables	(1,258,069)	65,518
Increase/(decrease) in tax liabilities	(3,071)	(311,853)
Increase/(decrease) in provisions	141,432	78,674
Net cash from operating activities	3,543,526	6,319,066

Non-cash financing and investing activities:

During the year the economic entity acquired plant and equipment with an aggregate value of $273,081 (2011: $277,123) by means of finance leases. These acquisitions are not reflected in the statement of cash flows.

NOTES TO THE FINANCIAL STATEMENTS (continued)

	2012 $	2011 $
31: EARNINGS PER SHARE		
Profit	1,249,380	(10,337,786)
Earnings used in the calculation of basic EPS	1,249,380	(10,337,786)
Earnings used in the calculation of dilutive EPS	1,249,380	(10,337,786)
Weighted average number of ordinary shares outstanding during the year used in calculation of basic EPS	52,929,356	52,891,490
Weighted average number of options outstanding	-	-
Weighted average number of ordinary shares outstanding during the year used in calculation of dilutive EPS	52,929,356	52,891,490
Earnings per share:		
Basic earnings per share (cents)	2.4	(19.5)
Diluted earnings per share (cents)	2.4	(19.5)
Earnings per share from discontinued operations:		
Basic earnings per share (cents)	(1.9)	(15.6)
Diluted earnings per share (cents)	(1.9)	(15.6)

32: BUSINESS COMBINATIONS

During the year, Probiotec Limited ("the Company") acquired the 50% of shares held by SP Health Co Pty Ltd in the Probiotec BLC Pty Limited ("PBLC") joint venture. As a result of this acquisition, the Company now holds 100% of the shares of PBLC. PBLC produces weight loss products under the "Biggest Loser Club" brand under an exclusive license. The acquisition of PBLC was effective from 15 September 2011. No part of the operations of PBLC have or are planned to be disposed of as part of the combination.

	Recognised on acquisition $
Property, plant and equipment	1,622
Deferred tax assets	5,400
Inventories	561,140
Intangible assets	499,648
Cash and cash equivalents	555,906
Trade and other receivables	824,938
Trade and other payables	(1,248,654)
Net identifiable assets and liabilities	1,200,000
Goodwill on acquisition	-
Consideration Paid*	(1,200,000)
	(1,200,000)

*Cash consideration of $600,000 paid. Balance of consideration paid represents fair value of the existing 50% ownership of PBLC at acquisition date. There is no contingent consideration payable under the acquisition agreement.

Fair value of investment

A gain of $233,376 has been recognised based on the fair value of the existing 50% ownership interest. This amount is included in other income in the statement of comprehensive income.

Goodwill

No goodwill resulted from this combination.

Revenue and profit contribution

The combination was effective 15 September 2011. Revenue would have been an additional $559,517 for the year and profit have have been an additional $41,098 if the combination had occurred at the start of the period. The incremental impacts on revenue and profit for the half year as a result of this combination were $652,932 and $64,098 respectively. Acquisition costs incurred in relation to this business combination in the amount of $97,894 were expensed during the year. These costs are included in administrative and other expenses in the statement of comprehensive income.

33: COMPANY DETAILS

The registered office of the company is:
Probiotec Limited, 83 Cherry Lane, Laverton North VIC 3026

The principal places of businesses are:
83 Cherry Lane, Laverton VIC
36 Bolong Road, Bomaderry NSW
35 Norfolk Avenue, South Nowra NSW
Finnabair Industrial Park, Dundalk, IRE

34: FINANCIAL INSTRUMENTS

Financial Risk Management

The Group's financial instruments consist mainly of receivables, payables, bank loans and overdrafts, finance leases, loans from related parties, cash and short-term deposits.

The Board of Directors has overall responsiblity for establishment and oversight of the risk management framework. The Board has established the Audit and Risk Management Committee, which is responsible for approving and reviewing the Group's financial risk management strategy and policy. The Group manages its exposure to key financial risks in accordance with the Group's risk management policy approved by the Board of Directors to enable the risks to be balanced against appropriate rewards for the taking and managing of the risks.

Risk management policies are established to identify, assess and control the risks which affects its business and are reviewed regularly to reflect changes in market conditions and the Group's activities.

NOTES TO THE FINANCIAL STATEMENTS (continued)

The Audit and Risk Committee overseas how management monitors compliance with the Group's risk management policies and procedures including the review of the adequacy of the risk management framework with respect to the risks faced by the Group.

Financial Risks

The main risks the Group is exposed to through its financial instruments are foreign currency risk, interest rate risk, liquidity risk and credit risk.

(a) Market risk

(i) Foreign exchange risk

The Group is exposed to foreign exchange risk arising from various currency exposures when it undertakes sale and purchase of goods and services in currencies other than the Group's measurement currency, primarily with respect to the British Pound, US dollar and the Euro. The Group seeks to mitigate the effect of its foreign currency exposure by maintaining foreign currency bank accounts that match the cash flows generated from and used by the underlying foreign currency transactions.

There has been no change to the Group's exposure to foreign currency risk or the manner in which the Group manages and measures the risk from previous period.

The Group's exposure to foreign currency risk at the reporting date was as follows:

	Consolidated Group					
2012	GBP $	NZD $	USD $	EUR $	CNY $	HKD $
Financial Assets						
Trade and other receivables	684,939	274,436	83,227	154,444	-	-
Financial Liabilities						
Trade and other payables	161,465	1,121	764	200,388	-	-
Net exposure	**523,474**	**273,315**	**82,463**	**(45,944)**	**-**	**-**
2011						
Financial Assets						
Trade and other receivables	754,710	65,826	174,902	166,342	80,651	181,781
Financial Liabilities						
Trade and other payables	362,945	9,515	53,592	150,473	131,487	90,289
Net exposure	**391,765**	**56,311**	**121,310**	**15,869**	**(50,836)**	**91,492**

Sensitivity analysis

Based on the financial instruments held as at 30 June 2012, a 10% strengthening of Australian dollar against GBP, 15% strengthening of Australian dollar against the New Zealand dollar (NZD), 10% strengthening of Australian dollar against US dollar, 10% strengthening of Australian Dollar against EUR, 10% strengthening of Australian dollar against Hong Kong Dollar (HKD) and 10% strengthening of Australian dollar aganist Chinese Yuan (CNY) at 30 June would have increased / (decreased) profit or loss and equity by the amounts shown below. This analysis assumes that all other variables remain constant. The analysis is performed on the same basis for 2011.

	Profit $	Equity $
2012		
GBP	(47,589)	-
NZD	(35,650)	-
US dollars	(7,497)	-
EUR	4,177	-
HKD	-	-
CNY	-	-
2011		
GBP	(35,615)	-
NZD	(7,345)	-
US dollars	(11,028)	-
EUR	(1,443)	-
HKD	(8,318)	-
CNY	4,621	-

A 10% weakening of Australian dollar against GBP, 15% weakening of Australian dollar against NZD, 10% weakening of Australian dollar against US dollar, 10% weakening of Australian dollar against EUR, 10% weakening of Australian dollar aganist Hong Kong dollar (HKD) and 10 weakening of Australian dollar against Chinese Yuan (CNY) at 30 June would have the equal but opposite effect on GBP, US dollar and NZD to the amount shown above on the basis that other variables remain constant.

(ii) Interest rate risk

The Group's exposure to market interest rates relates primarily to the Group's long-term debt obligations. The level of debt is disclosed in note 20. Borrowings issued at variable rates expose the Group to cash flow interest rate risk. Borrowings issued at fixed rates expose the Group to fair value interest rate risk.

The Group constantly analyses its interest rate exposure. The Group's current approach is to maintain approximately 10% - 50% of its borrowings at fixed rate using floating-to-fixed interest rate swaps and/or fixed rate leasing to achieve this. Generally, the Group raises long-term borrowings at floating rates and swaps them into fixed rates that are lower than those available if the Group borrowed at fixed rates directly. Under the interest rate swaps, the Group agrees with other parties to exchange, at specified intervals (mainly quarterly), the difference between fixed contract rates and floating-rate interest amounts calculated by reference to the agreed notional principal amounts. These swaps are designated to hedge the underlying debt obligations. During 2011 and 2012, the Group's borrowings at variable rates were denominated in Australian Dollars.

NOTES TO THE FINANCIAL STATEMENTS (continued)

As at the reporting date, the Group had the following financial assets and liabilities exposed to variable interest rate risk:

2012	Weighted average interest rate %	Floating interest rate maturing: 1 year or less $	Over 1 to 5 years $	More than 5 years $	Total $
Financial assets:					
Cash	2.90	193,388	-	-	193,388
Total financial assets		193,388	-	-	193,388
Financial Liabilities:					
Loans and overdraft	7.49	20,915,968	150,000	-	21,065,968
Total financial liabilities		20,915,968	150,000	-	21,065,968
Net exposure		**(20,722,580)**	**(150,000)**	**-**	**(20,872,580)**
2011					
Financial assets:					
Cash	2.90	938,107	-	-	938,107
Total financial assets		938,107	-	-	938,107
Financial Liabilities:					
Loans and overdraft	6.70	26,341,358	250,000	-	26,591,358
Total financial liabilities		26,341,358	250,000	-	26,591,358
Net exposure		**(25,403,251)**	**(250,000)**	**-**	**(25,653,251)**

(b) Liquidity risk

Liquidity risk is the risk that the Group may encounter difficulties rasing funds to meet commitments associated with financial instruments such as borrowing repayments.

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of available funding through an adequate amount of committed credit facilities such as bank overdrafts, bank loans and finance leases.

The Group manages liquidity risk by continuously monitoring forecast and actual cash flows and to have sufficient liquidity to meet its liabilities when due.

In addition, the Group had access to approximately $15.8 million undrawn credit facilities available for immediate use at the reporting date which would further reduce the liquidity risk. For further details see note 30(a).

Maturities of financial liabilities

	Consolidated Group				
2012	Carrying amount $	Total contractual cash flows $	Less than 6 months $	6 - 12 months $	1 - 5 years $
Non-derivatives financial liabilities					
Trade and other payables	10,213,722	10,213,722	9,892,722	321,000	-
Fixed borrowings	2,763,434	3,046,752	513,075	513,075	2,020,602
Variable borrowings	21,065,968	22,619,870	1,650,343	4,931,543	16,037,984
	34,043,124	35,880,344	12,056,140	5,765,618	18,058,586
2011					
Non-derivatives financial liabilities					
Trade and other payables	11,471,790	11,471,790	11,471,790	-	-
Fixed borrowings	2,712,868	3,081,605	419,140	419,140	2,243,325
Variable borrowings	26,591,358	31,032,116	7,287,556	7,287,556	16,457,004
	40,776,016	45,585,511	19,178,486	7,706,696	18,700,329

(c) Credit risk

Credit risk arises from the financial assets of the Group, which comprise cash and cash equivalents as well as credit exposures to customers, including outstanding receivables from subsidiaries and financial guarantees given to entities within the Group. The Group's exposure to credit risk arises from potential default of the counter party, with a maximum exposure equal to the carrying amount of these instruments. Exposure at reporting date is addressed in Note 12 .

The Group's policy is to trade with recognised and credit-worthy third parties and as such no collateral is required. The Group manages its credit risk by assessing the credit quality and financial position of its customers including past experience and other factors. In addition, receivable balances are monitored on an ongoing basis minimising the exposure to bad debts. The Group has also taken out a credit insurance policy that applies to all approved debtors. This policy provides insurance for 90% of the invoiced value outstanding based on pre-defining maximum credit limits agreed between the group and the insurer.

(d) Price risk

The Group is not exposed to any commodity and equity securities price risk. Most of the raw materials are sourced through importing agents and major suppliers in the local milk powder industry and the Group does not actively trade in equity investments.

(e) Fair values

The fair values of loans and amounts due are determined by discounting the cash flows, at market interest rates of similar borrowings, to their present value. For forward exchange contracts the fair value is the recognised unrealised gain or loss at reporting date determined from the current forward exchange rates for contracts with similar maturities.

For other assets and other liabilities the fair value approximates their carrying value. No financial assets and financial liabilities are readily traded on organised markets in standardised form other than listed investments, forward exchange contracts and interest rates swaps. Financial assets where the carrying amount exceeds fair values have not been written down as the economic entity intends to hold these assets to maturity.

	2012 Carrying Amount $	2012 Net Fair Value $	2011 Carrying Amount $	2011 Net Fair Value $
Financial Assets				
Trade & other current receivables	8,446,915	8,446,915	10,250,305	10,250,305
Cash	193,388	193,388	938,107	938,107
	8,640,303	8,640,302	11,188,412	11,188,412
Financial Liabilities				
Trade & others payables	10,213,722	10,213,722	11,471,790	11,471,790
Short term borrowings	20,915,968	20,915,968	26,341,358	26,341,358
Long term borrowings	150,000	150,000	250,000	250,000
Lease liability	2,763,434	2,763,434	2,712,868	2,712,868
	34,043,124	34,043,124	40,776,016	40,776,016

Fair values are materially in line with carrying values for all financial assets and liabilities.

35: PARENT ENTITY INFORMATION

The following details information related to the parent entity, Probiotec Limited, at 30 June 2012.

The information presented here has been prepared using consistent financial statements.

	2012 $	2011 $
Current assets	43,300,914	39,726,609
Non-current assets	26,197,619	20,292,336
Total Assets	**69,498,533**	**60,018,945**
Current Liabilities	26,168,552	26,091,111
Non-current liabilities	4,139,900	5,483,849
Total Liabilities	**30,308,452**	**31,574,960**
Contributed equity	35,072,269	36,581,517
Retained earnings	1,573,936	(9,652,138)
Equity Compensation Plan	(1,385,750)	(2,894,998)
Other reserve	3,929,626	4,409,605
Total equity	**39,190,081**	**28,443,986**
Profit / (loss) for the year	(6,336,147)	(16,437,907)
Other Comprehensive income for the year	192,771	-
Total comprehensive income for the year	**(6,143,376)**	**(16,437,907)**

The parent company has not guaranteed any loans held by its subsidiaries other than as part of the cross guarantees set out in Note 21 (d).

The parent entity is subject to contractual obligations in regards to the group's interest bearing liabilities as detailed in note 21. All finance leased held by the group (see note 27) are held by the parent entity.

36: SUBSEQUENT EVENTS

There has not been any matter or circumstance that has arisen since the end of the financial year that has significantly affected or may significantly affect, the consolidated entity's operations, the results of those operations, or the consolidated entity's state of affairs in financial years after the financial year.

37: SEGMENT INFORMATION

(a) Description of segments

Management has determined the operating segments based on reports reviewed by the executive management committee for making strategic decision. The executive management committee comprises the chief executive officer, chief financial officer and divisional managers. The committee monitors the business based on product and geographic factors and have identified 5 reportable segments.

Pharmaceuticals and consumer health

The pharmaceuticals and consumer health segment involves the sale of branded pharmaceutical products (both owned and licensed brands) along with the sale of a range of weight management products throughout Australia.

Contract manufacture

The Contract manufacturing segment involves the contract manufacturing of pharmaceutical, food and animal nutrition products on behalf of domestic and international pharmaceutical and food companies.

Nutritional products

The nutritional products segment is involved in the sale of human and animal nutrition products along with the sale of ingredients and additives for use in the pharmaceutical and food industries.

Export sales

The export sales segment is involved in the sale of products to markets outside of Australia. Product sales included in this segment are excluded from other segment figures.

Research and Development

The Research and Development segment is involved in the research and development of a range of innovative products and drugs for both domestic and international markets. This segment also involves the development of intellectual property to support the commercialisation of product in development by undertaking research, clinical trials, regitartions and other activities.

Business Segments	Segment name
Segment 1	Pharmaceuticals and consumer health
Segment 2	Contract manufacturing
Segment 3	Nutritional products
Segment 4	Export sales
Segment 5	Research & Development

NOTES TO THE FINANCIAL STATEMENTS (continued)

	Segment 1 $	Segment 2 $	Segment 3 $	Segment 4 $	Segment 5 $	Consolidated $
Year ended 30 June 2012						
Revenue from discontinued operations	-	-	-	418,814	-	418,814
Revenue from external customers	35,706,162	17,514,134	4,484,168	8,341,725	-	66,046,189
Total segmental revenue	35,706,162	17,514,134	4,484,168	8,760,539	-	66,465,002
Loss from discontinued operations		-	-	(979,870)	-	(979,870)
Impairment costs - continuing operations	-	-	-	(1,245)	-	(1,245)
Segmental profit from continuing operations	6,791,353	2,024,184	710,068	987,065	(2,183,790)	8,328,880
Total segmental profit	6,791,353	2,024,184	710,068	5,951	(2,183,790)	7,347,765
Interest						(2,011,984)
Unallocated other income						92,010
Unallocated corporate expenses						(4,170,046)
Total unallocated income / (expense)						(6,090,020)
Profit from continuing activities before income tax						2,237,617
Loss from discontinued operations before income tax						(979,870)
						1,257,747
Year ended 30 June 2011						
Revenue from discontinued operations	-	-	-	1,713,753	-	1,713,753
Revenue from external customers	38,307,241	16,779,503	7,184,150	9,499,251	-	71,770,145
Total segmental revenue	38,307,241	16,779,503	7,184,150	11,213,004	-	73,483,898
Loss from discontinued operations	(250,000)	-	(3,754,667)	(5,929,867)	-	(9,934,534)
Impairment costs - continuing operations	-	-	-	(3,115,527)	-	(3,115,527)
Segmental profit from continuing operations	6,971,517	2,252,274	518,451	(536,009)	(1,560,962)	7,645,271
Total segmental profit	6,721,517	2,252,274	(3,236,216)	(9,581,403)	(1,560,962)	(5,404,790)
Interest						(2,277,535)
Unallocated other income						365,894
Unallocated corporate expenses						(4,355,128)
Total unallocated income / (expense)						(6,266,769)
Loss from continuing activities before income tax						(1,737,025)
Loss from discontinued operations before income tax						(9,934,534)
						(11,671,559)

	2012 $	2011 $
(b) Reconciliation of segmental revenue to total revenue		
Segmental revenue	66,465,002	73,483,898
Interest received	119,657	111,716
Total revenue	66,584,659	73,595,614

(c) Segment revenue

Sales between segments (if they occur) are carried out at arm's length and are eliminated on consolidation. The revenue from external parties reported to the board is measured in a manner consistent with that in the statement of comprehensive income.

Revenues from external customers are derived from the sale of products on both a wholesale and business-to-business basis from each of the business segments outlined earlier in this note. A breakdown of revenue is provided in the tables above.

(d) Segment profit

The board assesses the performance of the operating segments based on a measure of adjusted EBIT. This measurement basis excludes the effects of non-recurring expenditure from the operating segments such as restructuring costs, legal expenses and goodwill impairments when the impairment is the result of an isolated, non-recurring event. This measurement basis also exlcudes the effects of any non-recurring items of revenue or income. Interest income and expenditure are not allocated to segments, as this type of activity is driven by the central treasury function, which manages the cash position of the group.

(e) Entity wide information

The gross revenue in each region where significant export revenue is achieved for the year was:

	Australia $	New Zealand $	European Union $	United States of America $	Other $
Gross Revenue for year ended 30 June 2012	57,185,897	1,257,331	6,893,480	574,804	553,490
Gross Revenue for year ended 30 June 2011	61,886,812	2,076,093	7,671,060	384,081	1,465,852

Revenues of approximately $10,371,556 and $8,672,626 (2011: $10,611,068 and $7,751,536) are derived from two major external customers included in the pharmaceutical and consumer health and contract manufacturing segments respectively.

(f) Segment assets

No disclosure of segment assets has been made as this information is not provided to the chief decision maker on a regular basis.

DIRECTORS' DECLARATION

PROBIOTEC LIMITED AND ITS CONTROLLED ENTITIES

ACN 075 170 151

DECLARATION BY DIRECTORS

The directors of the company declare that:

1. The financial statements, comprising the statement of comprehensive income, statement of financial position, statement of cash flows, statement of changes in equity, accompanying notes, are in accordance with the *Corporations Act 2001* and:
   (a) comply with Accounting Standards and the *Corporations Regulations 2001*; and
   (b) give a true and fair view of the financial position as at 30 June 2012 and of the performance for the year ended on that date of the consolidated entity.

2. The company has included in the notes to the financial statements an explicit and unreserved statement of compliance with International Financial Reporting Standards.

3. In the directors' opinion, there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

4. The remuneration disclosures included in pages 21 to 28 of the directors' report (as part of audited Remuneration Report), for the year ended 30 June 2012, comply with section 300A of the *Corporations Act 2001*.

5. The directors have been given the declarations by the chief executive officer and chief financial officer required by section 295A.

This declaration is made in accordance with a resolution of the Board of Directors and is signed for and on behalf of the directors by:

Charles Wayne Stringer
Richard Kuo

Dated at Laverton this 28th day of August 2012

INDEPENDENT AUDITOR'S REPORT

TO THE MEMBERS OF PROBIOTEC LIMITED

MOORE STEPHENS
ACCOUNTANTS & ADVISORS

Level 10, 530 Collins Street
Melbourne VIC 3000

T +61 (0)3 8635 1800
F +61 (0)3 8102 3400

www.moorestephens.com.au

INDEPENDENT AUDITOR'S REPORT
TO THE MEMBERS OF PROBIOTEC LIMITED

Report on the Financial Report

We have audited the accompanying financial report of Probiotec Limited, which comprises the statement of financial position as at 30 June 2012, the statement of comprehensive income, the statement of changes in equity and the statement of cash flows for the year then ended, notes comprising a summary of significant accounting policies and other explanatory information, and the directors' declaration of the consolidated entity comprising the company and the entities it controlled at the year's end or from time to time during the financial year.

Directors' Responsibility for the Financial Report

The directors of the company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error. In Note 1, the directors also state, in accordance with Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial statements comply with *International Financial Reporting Standards*.

Auditor's Responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. Those standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance about whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Independence

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of Probiotec Limited would be the same terms if given to the directors as at the time of this auditor's report.

INDEPENDENT AUDITOR'S REPORT (continued)

MOORE STEPHENS
ACCOUNTANTS & ADVISORS

Opinion

In our opinion:

a) the consolidated financial report of Probiotec Limited is in accordance with the *Corporations Act 2001*, including:

   i) giving a true and fair view of the company's financial position as at 30 June 2012 and of its performance for the year ended on that date; and

   ii) complying with Australian Accounting Standards and the *Corporations Regulations 2001*; and

b) the financial report also complies with *International Financial Reporting Standards* as disclosed in Note 1.

Report on the Remuneration Report

We have audited the Remuneration Report included in pages 7 to 15 of the directors' report for the year ended 30 June 2012. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Opinion

In our opinion, the Remuneration Report of Probiotec Limited for the year ended 30 June 2012 complies with section 300A of the *Corporations Act 2001*.

Moore Stephens

MOORE STEPHENS
Chartered Accountants

Nick Michael
Partner

Melbourne

28 August 2012


low carb
RAPID
celebrityslim
7 DAY
Ladybird
figure
Aqueous Lotion
VITAMIN C
fish oil 1000mg

OTHER INFORMATION REQUIRED BY ASX LISTING RULES

The information in this section is current as at the 17th September 2012.

Substantial Holders in the entity, as disclosed in substantial holding notices given to the entity

Charles Wayne Stringer	8,675,786 fully paid ordinary shares
Vintage Capital Pty Ltd (ACN 116 337 592)	4,400,000 fully paid ordinary shares

Holders of each class of equity securities

Security Classes	Holders	Total Units
Fully Paid Ordinary	1,518	52,929,356

Voting rights attached to each class of equity securities

Each fully paid ordinary share is entitled to one vote when a poll is called, otherwise each member present at a meeting or by proxy has one vote on a show of hands.

Distribution schedule of number of holders of each class of equity securities

Security Classes	Holdings Ranges	Holders	Total Units	%
Fully Paid Ordinary	1-1,000	252	137,040	0.259
	1,001-5,000	572	1,487,465	2.810
	5,001-10,000	260	2,059,551	3.891
	10,001-100,000	366	11,002,471	20.787
	100,001-99,999,999,999	68	38,242,829	72.253
	Totals	**1,518**	**52,929,356**	**100.000**

Holders with less than a marketable parcel of the main class of securities

At the date of this report, a marketable parcel of fully paid ordinary shares was 1,492 or more shares.

Security Classes	Holdings Ranges	Holders	Total Units	%
Fully Paid Ordinary	0 – 1,492	386	299,243	0.565
	1,493 – 99,999,999,999	1,132	52,630,113	99.435
	Totals	**1,518**	**52,929,356**	**100.000**

Company secretaries

The secretary of Probiotec Limited is:

Mr. Jared Stringer

Full details and qualifications for the secretary can be found in the Directors' Report.

20 largest holders of each class of quoted equity securities

At the date of this report, there is only one class of quoted equity securities, being fully paid ordinary shares. The 20 largest holders of this class at the date of this report were:

Holder Name	Holding	%
INSTON PTY LTD (STRINGER FAMILY A/C)	4,866,676	9.195
VINTAGE CAPITAL PTY LTD	4,461,110	8.428
MR CHARLES WAYNE STRINGER	2,438,574	4.607
UBS NOMINEES PTY LTD	2,434,567	4.600
GANTER CORPORATION PTY LTD (GANTER FAMILY A/C)	1,993,015	3.765
VBS INVESTMENTS PTY LTD	1,204,260	2.275
TRIFERN PTY LTD (SUPER FUND ACCOUNT)	1,171,589	2.213
MR SCOTT JOHNSTON (JOHNSTON FAMILY S/F A/C)	1,018,255	1.924
INGOT CAPITAL INVESTMENTS PTY LTD	1,000,000	1.889
INSTON PTY LTD (STRINGER SUPER FUND A/C)	976,295	1.845
BRAZIL FARMING PTY LTD	810,581	1.531
KOONTA PTY LTD (THE TEDDER FAMILY A/C)	801,224	1.514
NAVIGATOR AUSTRALIA LTD (MLC INVESTMENT SETT A/C)	762,700	1.441
HOLTEX PTY LIMITED (BUCKERIDGE SUPER FUND A/C)	754,924	1.426
TRUST COMPANY SUPERANNUATION SERVICES LIMITED (SPARXX S/F A/C)	712,069	1.345
INVESTMENT CUSTODIAL SERVICES LIMITED (R A/C)	668,223	1.262
TAYLOR CO PTY LTD (PETER TAYLOR SUPER FUND A/C)	636,883	1.203
HOLTEX PTY LTD (BUCKERIDGE S/F A/C)	593,761	1.122
J P MORGAN NOMINEES AUSTRALIA LIMITED	556,327	1.051
MR HENRY ATHOLL CUNNINGHAM ROBERTSON	506,277	0.957
	28,367,310	**53.595**

Registered Office and principal administrative office

The registered office and principal administrative office for Probiotec Limited is:

83 Cherry Lane
Laverton North
Victoria 3026
Ph: (03) 9278 7555

Register of securities, register of depositary receipts and other facilities for registration or transfer

All registers of securities, registers of depositary receipts and other facilities for registration or transfer are kept at:

Boardroom Limited
Level 7, 207 Kent Street
Sydney NSW 2000
Ph: (02) 9290 9600
Fax: (02) 9279 0664

Other stock Exchanges on which entity's securities are quoted

Securities in Probiotec Limited are not quoted on any other stock exchange other than the Australian Stock Exchange (ASX).

Restricted and Escrowed Securities

At the date of this report no securities were subject to escrow.

Unquoted Equity Securities

Security Classes	Holders	Total Units
Fully Paid Ordinary – issued under Employee incentive schemes	18	3,065,000

On market buy-back

As at the date of this report, there is no current on market buy-back.

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Probiotec **Annual Report 2012**

Head office
Probiotec Limited
83 Cherry Lane, North Laverton,
VIC, Australia, 3026

www.probiotec.com.au